

UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

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IN RE: EQUAPHOR INCORPORATED, : Case No. 10-20490-SSM
:
Debtor. : (Chapter 7)
- - - - - x

Monday, May 2, 2011
U.S. Bankruptcy Court
Alexandria, Virginia

The above-entitled matter came on to be heard before

THE HONORABLE STEPHEN S. MITCHELL, Judge in and for the

United States Bankruptcy Court, for the Eastern District of

Virginia, Alexandria Division, beginning at approximately

11:00 o'clock, a.m.

* * * * *

APPEARANCES:

On behalf of the Debtor:

STEVEN RAMSDELL, ESQUIRE

On behalf of Chapter 7 Trustee:

KEVIN MCCARTHY, ESQUIRE

On behalf of Frederick Bamber and Harry George:

JAMES SCHROLL, ESQUIRE

THOMAS G. SHAPIRO, ESQUIRE

On behalf of Kobayashi Ventures, LLC:

JAMES REYNOLDS, ESQUIRE

JEFFREY SCHWABER, ESQUIRE

On Behalf of Carotek, Inc. And Event Capture
Systems, LLC:

DAVID SWAN, ESQUIRE

KENNETH MISKEN, ESQUIRE

THAD ADAMS, ESQUIRE (via telephone)

* * * * *

C O N T E N T S

WITNESS	DIRECT	CROSS	REDIRECT	RECROSS
KEVIN McCARTHY		5	40	44
		(Shapiro)	(McCarthy)	

JAMES DECHMAN	47	65	82	
	(McCarthy)	(Miskin)	(Shapiro)	

JOHN B. DOHERTY	114	121	135	
	(McCarthy)	(Miskin)	McCarthy)	

121
(Shapiro)

CLARENCE E. SPIVA	136	139	
	(McCarthy)	(Miskin)	

140
(Shapiro)

E X H I B I T S

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1 THE COURT: Good morning. Please be seated. We
2 will call our 11:00 o clock matter.

3 THE CLERK: We have items number one and two,
4 Equaphor, Incorporated, Case Number 10-20490.

5 THE COURT: Will counsel please put their appearance
6 on the record?

7 MR. MCCARTHY: Good morning, Your Honor. Kevin
8 McCarthy, the trustee and the attorney for the trustee.

9 MR. SCHROLL: Good morning, Your Honor. James
10 Schroll and Thomas Shapiro on behalf of Harry George and
11 Frederick Bamber.

12 MR. ADAMS: And Your Honor, this is Thad Adams in
13 Charlotte, North Carolina, appearing by telephone.

14 THE COURT: Just a second, Mr. Adams. We need to
15 get the volume up on the phone system here. Okay. In the
16 meanwhile.

17 MR. REYNOLDS: Your Honor, James Reynolds on behalf
18 of Kobayashi Ventures, LLC. I also have with me as co-
19 counsel Jeffrey Schwaber from the law firm of Stein Sperling.

20 MR. SWAN: Good morning, Your Honor. David Swan for
21 Carotex and ECS. With me is Ken Miskin and on the phone is
22 Thad Adams.

23 THE COURT: Mr. Adams, are you on the phone?

24 MR. ADAMS: Yes, Your Honor, I am.

25 THE COURT: Okay. Thank you.

1 MR. RAMSDELL: Steven Ramsdell for the debtor.

2 THE COURT: Okay. Thank you, Mr. Ramsdell.

3 I believe where we were when we adjourned on last
4 week was that Mr. McCarthy was on the witness stand and we
5 were in the middle of cross examination by Mr. Miskin.

6 MR. SHAPIRO: I think I was cross examining.

7 THE COURT: You were examining. I m sorry, Mr.
8 Shapiro.

9 Whereupon,

10 KEVIN MCCARTHY

11 was resumed as a witness and, having been previously duly
12 sworn, was examined and testified as follows:

13 CROSS EXAMINATION

14 BY MR. SHAPIRO: (Resumed)

15 Q Good morning, Mr. McCarthy.

16 A Good morning, Mr. Shapiro.

17 Q You were asked last week some questions about the
18 legal bills that underlay the claims by the three law firms
19 or four law firms that are claims against the estate, and I
20 won t ask you to repeat what was asked then.

21 Would you agree that if any of the work underlying
22 those bills that make up the law firm claims was done in
23 whole or in part on behalf of Kobayashi and Dechman, who were
24 parties to the Carotex litigation, that it wouldn t be proper
25 to charge all of those fees to Equaphor?

1 A Yes.

2 Q And if it wasn t proper to charge all the fees to
3 Equaphor then those claims would be subject to challenge,
4 would they not, in the bankruptcy proceeding?

5 A Yes.

6 Q And is it correct that you do not know whether or
7 not Kobayashi or Mr. Dechman were charged any legal fees in
8 the Carotex litigation after the point in time when the
9 patents were sold to Equaphor in September 2009?

10 A I don t know that. I do know after our cross
11 examination or my cross examination last week, I went back
12 and I had in fact received the bills, and I don t think I d
13 remembered that at the time when you examined me; and I did
14 give you a cover sheet showing the bills were transmitted to
15 me, and I ve since rechecked and the bills all say Equaphor
16 on them. But whether or not there were additional bills
17 going to Kobayashi and Dechman at the same time I don t know.

18 Q And whether or not the work that was charged to
19 Equaphor benefitted Equaphor, Kobayashi and Mr. Dechman you
20 don t know; is that right?

21 A I guess I don t know if there would have been an
22 indirect benefit, as well.

23 Q Well, Kobayashi and Dechman were parties to the
24 litigation after September 2009 and continued to be parties;
25 didn t they?

1 A They did.

2 Q And you ve never seen the underlying bills with any
3 itemization of what work was done or what days, by whom, that
4 sort of thing?

5 A Other than the bills that were presented to
6 Equaphor that became claims within this estate. I did look
7 at those invoices.

8 Q And what was in the invoices? Were there just
9 bills stating, for services rendered, X dollars were owed?

10 A It was itemized. My focus though was on to whom
11 the bill was addressed, and I probably looked at the
12 substance but not in much detail, and the reason is because
13 you told me that was an issue and so I wanted to check out at
14 least to whom the bills were addressed and whether or not on
15 the face of them they looked to be appropriate claims against
16 Equaphor.

17 Q But the work that was reflected in those bills
18 would benefit all of the defendants that were defendants in
19 damage claims by Carotex?

20 A I would expect that to be the case.

21 Q But you still don t know whether Mr. Dechman or
22 Kobayashi paid any part of that work?

23 A No.

24 Q You testified last week that PaperTech offered to
25 pay the estate \$60,000 for the patents?

1 A Yes.

2 Q And did you attempt to negotiate a higher price
3 with PaperTech?

4 A No; but when I made the outline of the deal, I
5 sent you an e-mail to keep you informed and I sent them an
6 e-mail to keep their attorney, Mike Reynolds, to keep him
7 informed, as well, the idea being that - and I think I sent
8 David Swan an e-mail, as well - the idea being to keep
9 everybody informed; and whether I said, Do you want to bid
10 or not? I kind of doubt it at that point. But the idea was
11 if you want to bid more, you know, you may.

12 Q Did you do any evaluate of the payments to
13 Kobayashi that were made within one year prior to the
14 bankruptcy filing?

15 A I did in the sense of I got the asset purchase
16 agreement that was made and approved by the board in 2009 and
17 I made certain that the accounts receivable were on the list
18 that were attached to the asset purchase agreement because a
19 large group of payments made to - I get it a little bit
20 mixed up sometimes but I think in this case it probably was
21 Monitoring Technology, LLC.

22 The large group of payments made to Monitoring
23 Technology, LLC were accounts receivable that I was told
24 should have come to them but it came to the debtor because of
25 the way the accounts were set up among the customers, and I

1 verified that that appeared to be consistent with the
2 agreement.

3 Q I was going to come to that next. So, let me ask
4 you a question and then I ll go back to the Kobayashi
5 payments. Okay? I believe it was Monitoring Technology that
6 acquired the business assets of Equaphor other than the ones
7 that were sold to Cognex. Do you understand that to be the
8 case?

9 A Yes.

10 Q And that was in an acquisition, \$1.5 million, in
11 round numbers; correct?

12 A Yes.

13 Q And then that purchase - they paid a million-five
14 and part of what they got was the right to all the accounts
15 receivable, and I believe Exhibit 10 which is now in
16 evidence, one of the bankruptcy schedules, reflects that a
17 approximately \$988,000 was paid by Equaphor over to
18 Monitoring Technology during the preference period for
19 insider-related transactions?

20 A Yes.

21 Q And it s your understanding that was accounts
22 receivable that were paid over?

23 A Yes.

24 Q And you understand that that s part of the damage
25 claim that s asserted in the derivative action?

1 A Yes.

2 Q Now, going back to Kobayashi, Kobayashi was the
3 entity created by Mr. Dechman and Fiore for the purpose of
4 purchasing these patents; is that right?

5 A Yes.

6 Q To your understanding. And according to Exhibit
7 10, \$61,500 was paid over to Kobayashi by Equaphor during
8 the preference period. Do you recall that, sir?

9 A Sixty-one-five?

10 Q Yes.

11 A Not specifically; but I think it s in the statement
12 of financial affairs, and I definitely looked at that, got a
13 schedule of all of the payments to insiders within a year and
14 all the payments to non-insiders within 90 days and I looked
15 at them.

16 MR. SHAPIRO: Your Honor, it s in Exhibit 10, page,
17 Bates number 202, which is the Schedule of financial affairs.

18 BY MR. SHAPIRO:

19 Q And did you investigate what those payments were
20 for?

21 A Well, could I have back the - I have it in my bag.

22 THE COURT: Just a second. The exhibits are back in
23 chambers. My law clerk is going to get them.

24 THE WITNESS: Judge, may I go get my copy, too?

25 THE COURT: We re going to bring back the one that

1 should be on the witness stand.

2 THE WITNESS: I may have ended up with that.

3 THE COURT: Oh. Okay. Go ahead.

4 MR. SHAPIRO: Mr. Schroll took the liberty of taking
5 this out of your bag.

6 THE COURT: The witness has a copy. So, you can
7 just leave that.

8 BY MR. SHAPIRO:

9 Q It s at tab ten; and then, if you would turn to the
10 page. I think it s CAR202 within Exhibit 10.

11 A Okay. I see it.

12 Q Did you investigate what that \$61,500 was for?

13 A Those payments I think were part of the MSA - no.
14 I m sorry. Part of the asset - MSA was in 07. The asset
15 purchase agreement was in 09; and in 09, there was an -
16 as I recall, amidst the asset purchase agreement was a fee
17 that was permitted to be charged by Kobayashi for the purpose
18 of administering Equaphor s affairs with respect to the
19 patent. That s about as well as I can say it.

20 Q So, it was in September 2009 that Kobayashi sold
21 the patents to Equaphor; correct?

22 A I think the settlement may have been as of October.

23 Q Okay. And Equaphor was to pay Kobayashi
24 \$3,450,000?

25 A Correct.

1 Q And then on top of that it s your understanding
2 that Equaphor was required to pay Kobayashi some fees for
3 managing the patents that Kobayashi had just sold to
4 Equaphor?

5 A Correct.

6 Q And that s what the \$61,500 was?

7 A I think that s right.

8 Q Did you investigate whether that could be
9 recovered by the estate as a preference?

10 A Well, in the sense of verifying that payments
11 appeared to have been made in accordance with the asset
12 purchase agreement which was approved by the board and which
13 in turn flowed from the MSA in 07 which was approved by the
14 board; and once somebody - maybe Mr. Miskin asked me earlier
15 whether I d reviewed balance sheets. I did look at balance
16 sheets, as well. Again, I m not saying my level of analysis
17 was very detailed but I remember looking at a bottom line and
18 saying, oh, I guess they were solvent.

19 So, I considered those factors as part of, you
20 know, my looking at all of the payments that were made to
21 Kobayashi or Monitoring Technology. I was focusing on
22 primarily: Were the payments consistent with contracts that
23 were approved by the board and was there any obvious
24 insolvency at the time such that I might have wanted to take
25 a second look at that?

1 Q Apart from whether Kobayashi had a contract right
2 to the money, did you evaluate whether the 61,500 that was
3 paid during the preference period could be recovered by the
4 estate as a preference?

5 A You say apart from whether it was consistent with
6 the contract?

7 Q Yes.

8 A I don t think I did; no.

9 Q And if the estate could recover that money at
10 having been a preferential transfer then that s money that
11 would have been available to the estate to pay administrative
12 expenses, including expenses for defending the estate in the
13 Carotex litigation; is that right?

14 A Yes.

15 Q And the \$988,000 that was paid to Monitoring
16 Technology on account of accounts receivable, the money that
17 was paid over within a year of bankruptcy, that could be
18 recovered as a preference; could it not?

19 A I don t know. I don t think so. I mean, you
20 know, I -

21 Q Well, it was paid on account of a contract that
22 was signed in 2007; correct?

23 A Right. The way I understood your question, you
24 were asking me to conclude that they were preferential
25 payments. Certainly they could have been if all of the

1 elements of Section 547 had been satisfied.

2 Q Did you evaluate whether they were satisfied or
3 did you just simply decide that they were accounts receivable
4 that were required to be paid over by the 2007 contract?

5 A Well, as I said, there are two things I focused
6 on. One, was the company insolvent? I looked at some
7 balance sheets. It should have been insolvent in order for
8 there to be a recoverable preference. And then two, I looked
9 at the contract to see whether they were consistent with the
10 contract; talked to two of the board members from - well,
11 from all the way back to 07, Mr. Doherty and Mr. Spiva, as
12 well, about certain aspects of the deals. And based on all
13 of that, I didn't think that there was an obvious preference.

14 I don't say that somebody couldn't come to a
15 different conclusion but I think I had something reasonable
16 to go on in not pursuing that.

17 MR. SHAPIRO: May I have just a moment, Your Honor?

18 (Pause.)

19 BY MR. SHAPIRO:

20 Q If all or some part of the \$988,000 could have been
21 recovered as a preference then that would have brought money
22 into the estate that could have been used to pay for legal
23 costs in the Carotex litigation; correct?

24 A Yes.

25 Q Did you determine at what point Equaphor became

1 **insolvent?**

2 A I asked for a balance sheet as of September 26th
3 of 09 and I m not sure at this point why that was but I was
4 probably focusing on before the deal closed; and then I asked
5 for a balance sheet at the end of October of 09 and I think
6 I was focusing on after the deal closed. So - I actually
7 forgot your -

8 **Q All right. Did you determine at what point the**
9 **company became insolvent?**

10 A Oh. And both of those indicated that the company
11 was solvent.

12 **Q In September of 09?**

13 A And even after the deal, at least on paper.

14 **Q But how long after the deal? When did it become**
15 **insolvent?**

16 A September - well

17 **Q Do you know whether the company was insolvent at**
18 **the time it filed a voluntary petition in bankruptcy?**

19 A No, I don t. There would be a presumption of
20 insolvency during the 90 days before that.

21 **Q A presumption but you didn t evaluate whether the**
22 **financial condition of the company was such that it was**
23 **insolvent?**

24 A No.

25 **Q Are you aware that filing a petition in bankruptcy**

1 **divests shareholders of the right to bring or maintain a**
2 **derivative action?**

3 A I became aware of that.

4 **Q Have you seen the director s - the minutes of the**
5 **director s meeting when they decided to explore bankruptcy?**

6 A I have. I think it was attached to your
7 opposition.

8 MR. SHAPIRO: May I approach, Your Honor?

9 THE COURT: No. Pass it through the court security
10 officer. We will mark it as Bamber s Exhibit A.

11 MR. SHAPIRO: Exhibit A? The letter A did you
12 say?

13 THE COURT: The letter A.

14 (Bamber s Exhibit A
15 was marked for identification.)

16 MR. SHAPIRO: I offer this into evidence, Your
17 Honor.

18 MR. REYNOLDS: Your Honor, I ll object. There is no
19 foundation that Mr. McCarthy was present at the meeting. I
20 will object on hearsay but there s no foundation that he was
21 present at the meeting and that he can testify as to this.

22 THE COURT: Do you want to lay a foundation for its
23 admission?

24 MR. SHAPIRO: I ll have to call another witness.

25 I could call the director who s here in the room who was at

1 the meeting.

2 THE COURT: Okay. I ll let you examine right now,
3 subject to tying it up.

4 MR. SHAPIRO: Okay. Thank you.

5 BY MR. SHAPIRO:

6 Q The first time you saw these minutes was when you
7 saw the opposition to the motion for approval of compromise
8 and the sale?

9 A I think that s right.

10 Q If you look under paragraph number two,
11 Discussion, it says: The board discussed the offer sent by
12 Shapiro for the Bamber, George lawsuit. The consensus was
13 that this was an outrageous offer. Do you see that?

14 A I do.

15 Q And then at the bottom of the page it says the
16 board discussed filing for bankruptcy?

17 A Yes.

18 Q And then it says: An independent court-appointed
19 trustee would take over the company and manage the final
20 liquidation. The trustee could either sell or continue
21 litigation for the benefit of the creditors and
22 shareholders. Do you see that, sir?

23 A Yes.

24 Q And did you have discussion with counsel for the
25 company or any of the directors as to whether one of the

1 reasons they filed this voluntary petition in bankruptcy was
2 to try to eliminate the shareholder derivative case? Did you
3 have any discussion on that issue?

4 A Yes. It seems to me I was told by someone on that
5 side, whether it was one of the attorneys or Mr. Dechman,
6 that the shareholder derivative suit was - there wasn't
7 money to handle it and it helped propel the debtor into
8 bankruptcy.

9 Q Do you know who the defendants were in the share-
10 holder derivative suit?

11 A Well, I reviewed your complaint and the - Mr.
12 Spiva, Mr. Doherty, Molly Hale, I think Jim Dechman.

13 MR. SHAPIRO: I would like to offer the derivative
14 action complaint, Your Honor. I could testify as to its
15 authenticity, filed in Delaware, Chancery Court. I don't
16 know if there would be any objection to offering -

17 MR. MCCARTHY: I don't object to it, Your Honor.

18 MR. REYNOLDS: Your Honor, I don't object to the
19 exhibit being offered as a lawsuit that was filed in
20 Delaware; but as to the truth of the statements therein, I
21 would object.

22 THE COURT: Just being offered to show what the
23 contentions are and what's at play?

24 MR. SHAPIRO: Exactly, Your Honor.

25 THE COURT: We will mark it as Bamber's Exhibit B.

1 (Bamber s Exhibit B
2 was marked for identification.)

3 BY MR. SHAPIRO:

4 Q I sent you a copy of this complaint some time ago;
5 did I not, Mr. McCarthy?

6 A Yes.

7 Q And did you read it at that time?

8 A I did.

9 Q And you notice in the caption it says that Equaphor
10 is a nominal defendant?

11 A Yes.

12 Q And are you aware that means that no damages or
13 relief was sought from the company itself?

14 A I m aware of that.

15 Q Okay. So, the damages sought in this lawsuit were
16 sought from Mr. Dechman, Mr. Fiore, Monitoring Technology,
17 Kobayashi, Molly Hale, who was a director of the company,
18 correct, and Mr. Doherty and Mr. Spiva, and not from
19 Equaphor; correct?

20 A That you were not seeking damages from Equaphor, I
21 agree with that.

22 Q So, when someone told you there was no money to
23 defend the lawsuit, were they saying that Mr. Dechman, Fiore,
24 et cetera, did not have money to defend the lawsuit?

25 A The bylaws require indemnification of expenses,

1 including attorney fees; and as I understand it, that is
2 supposed to be made along the way. Now, there may be
3 discretion as to whether it can be made along the way but
4 it s a requirement of the bylaws that directors be
5 indemnified against expenses, including attorney fees so long
6 as they re found to be in good faith down the road.

7 I don t have the bylaws in front of me right now
8 but it was arguably a claim that was against the debtor in
9 terms of that.

10 **Q You testified last week, I think in answer to one**
11 **of my questions, that you didn t obtain books and records of**
12 **the company from Mr. Dechman or Monitoring Technology who**
13 **had them in his - you believed they were in his offices.**
14 **Did you see the bylaws yourself?**

15 A Well, yes. No. I looked at the bylaws. Sure.

16 **Q And how did you obtain a copy of the bylaws?**

17 A I obtained them from Mr. Dechman.

18 **Q So, the indemnification right would be a claim**
19 **that directors would have against the company; correct? It s**
20 **a claim you have?**

21 A It s certainly a claim, and I d like to have a copy
22 of the bylaws in front of me right now to refresh myself.
23 There at least was something in there that authorized -
24 well, I don t want to speculate. It was a claim. At this
25 point, without them in front of me, I can t tell you that it

1 is something that had to be paid as expenses were incurred or
2 not.

3 Q Well, whether it had to be paid or whether it s a
4 discretion of the board, it would be a claim against the
5 company, like a law firm claim or some other claim; right?

6 A Correct.

7 MR. SHAPIRO: Excuse me, Your Honor.

8 (Pause.)

9 BY MR. SHAPIRO:

10 Q You testified that you did look at balance sheets
11 of the company; correct?

12 A Yes.

13 Q Did you look at income statements? Did you look
14 at a set of financial statements that would be balance sheet,
15 income statement and cashflow that came together?

16 A I m not sure that I did look at income and
17 expenses.

18 MR. SHAPIRO: Could I ask the witness to be shown
19 this, Your Honor?

20 THE COURT: We will mark it as Bamber s Exhibit C.

21 (Bamber s Exhibit C
22 was marked for identification.)

23 MR. REYNOLDS: Your Honor, just to clarify, is this
24 being moved into evidence at this time?

25 THE COURT: I haven t heard a motion to admit it.

1 MR. REYNOLDS: Thank you.

2 BY MR. SHAPIRO:

3 Q I m showing you a document that says at the top
4 Equaphor Income Statement for the Month Ending November 30,
5 2010 and Year to Date. Have you seen that before?

6 A I don t recall having seen this before. It s
7 possible it was attached to something but I don t recall it
8 right now.

9 Q Do you have with you in your bag the financial
10 statements you obtained?

11 A I do.

12 THE WITNESS: Your Honor, I have a Redweld of two
13 folders. One is entitled, Documents I Received Before the
14 Compromise. The other, just to keep it straight in my own
15 mind, is Documents Received After the Compromise. If I
16 could have that with me, I might be able to respond better to
17 the questions.

18 MR. SHAPIRO: Maybe there s no objection, Your
19 Honor. I don t know if there s an objection. I would offer
20 it in evidence.

21 MR. REYNOLDS: Your Honor, if this document is being
22 offered into evidence, we don t know if Mr. - the question
23 is, has Mr. McCarthy seen this document before? And he
24 doesn t know.

25 THE COURT: I ll let Mr. McCarthy get his -

1 THE WITNESS: Thank you, Your Honor.

2 MR. SHAPIRO: Well, I would like to offer it whether
3 he s seen it or not, Your Honor, if there s no objection.

4 MR. REYNOLDS: There is an objection on hearsay and
5 there s no foundation for it at this point.

6 MR. SHAPIRO: Okay. I ll tie it up through another
7 witness or through myself, Your Honor.

8 (Pause.)

9 THE COURT: If you ll give Mr. McCarthy a moment so
10 he can look to see what he has.

11 (Pause.)

12 THE WITNESS: I think I can safely say I haven t
13 seen that before.

14 MR. SHAPIRO: May I question him subject to tying it
15 up later, Your Honor? I just have one question.

16 THE COURT: Okay. Go ahead.

17 BY MR. SHAPIRO:

18 **Q Do you see, Mr. McCarthy, in the list of expenses**
19 **in the bottom half of the page, there s an item, General**
20 **Legal Expenses, \$158,000 in November 2010 and \$803,540 year**
21 **to date?**

22 A Yes, sir.

23 **Q Were you aware that the company had spent \$803,000**
24 **on legal expenses in 2010?**

25 A I knew it was hundreds of thousands of dollars.

1 I m not sure I knew about the specific figure.

2 Q All right. Other than what you ve testified to
3 earlier, did you investigate whether these payments could be
4 recovered as a preference?

5 A Yes.

6 Q As you described earlier?

7 A Yes.

8 Q Is it your understanding that all of those expenses
9 were for the Carotex litigation?

10 A I think that s right.

11 Q And you are aware, are you not, sir, that the sale
12 of the patents to Equaphor is one of the transactions alleged
13 in the derivative complaint to have damaged Equaphor?

14 A Yes.

15 Q Now, there was also testimony last week about
16 \$249,000 paid to Stein Sperling during the preference period.
17 Do you recall that?

18 A Yes.

19 Q And you agree that that s a significant claim of
20 the estate?

21 A Potentially.

22 Q Did you look at the Stein Sperling invoices before
23 entering into the agreement with Kobayashi and Dechman?

24 A They were included in the attorney bills that I
25 looked at.

1 Q And I believe you testified - and see if I
2 understand you correctly, that your testimony was that your
3 analysis showed that the new value in ordinary course was a
4 small percentage of the \$249,000 and you thought there was a
5 substantial claim against Stein Sperling.

6 A I did, if all of the other elements of preference
7 were present; yes.

8 Q And any recovery on a preference claim against them
9 would have brought money into the estate that could have been
10 used to defend the Carotex litigation?

11 A Yes.

12 Q Now, under the proposed agreement we re here
13 discussing, all of Equaphor s claims against Carotex and the
14 other plaintiff in that case, ECS, are to be transferred to
15 Kobayashi along with the patents; correct?

16 A All of Equaphor s claims in what?

17 Q Against Carotex and ECS, any patent claims that
18 they have.

19 A Yes.

20 Q Whether it s against Carotex and ECS in the pending
21 litigation or any other party involved in the patents? All
22 the claims that Equaphor has are to be transferred to
23 Kobayashi along with the patents; is that right?

24 A Yes.

25 Q So, under this agreement, Equaphor is giving up any

1 **claims it has but it remains liable for any damage claims**
2 **that Carotex and ECS have asserted against Equaphor; correct?**

3 A Yes; I mean, to the extent they can be separated in
4 that fashion.

5 Q **What do you mean could be separated?**

6 A Some of the litigation is about whether or not the
7 patents are valid in the first place.

8 Q **I mean the damage claims, Carotex s claims for**
9 **damages.**

10 A Yeah, I think that s right. If there is a damage
11 claim, it remained against the estate.

12 Q **So, Equaphor, the estate, remains a party to that**
13 **litigation with no claims it s asserting but damage claims**
14 **against it will survive?**

15 A Yes.

16 Q **And part of the agreement is that Kobayashi will**
17 **pay any legal fees for Equaphor in that litigation?**

18 A Yes.

19 Q **And what is your understanding as to who will**
20 **represent Equaphor? Do you have any understanding?**

21 A Well, we don t have it in the agreement. I think
22 the understanding has been Stein Sperling by virtue of its,
23 you know, familiarity with the litigation would handle it.

24 Q **It would be up to Mr. Dechman and Kobayashi to**
25 **decide who would represent Equaphor?**

1 A And me.

2 Q And you? Does the agreement give you a say-so in
3 that?

4 A Well, it doesn't take it away.

5 Q Have you evaluated whether there's a conflict of
6 interest in having Equaphor represented by the same law firm
7 that represents Kobayashi and Dechman?

8 A Right. We didn't spell out who would be - I think
9 Stein Sperling - you know, there would be an issue there
10 because they are representing insiders, as well. We didn't
11 spell it out in the agreement. We simply said that the
12 litigation costs have to be handled or paid for by Kobayashi.

13 Q Do you recall you testified last week - and I can
14 show you the transcript - it's at page 17 - that you
15 thought that Kobayashi had reached an agreement with Stein
16 Sperling that it would handle the representation of Equaphor
17 at little or no cost to Kobayashi?

18 A Yes. I've heard that.

19 Q And who did you hear that from?

20 A Mr. Dechman.

21 Q So, they were going to be generous and undertake to
22 be responsible for Equaphor's legal fees but they worked out
23 a deal with Stein Sperling that would cost them little or
24 nothing; correct?

25 A Well, I think that's an argument.

1 Q Well, under the agreement, they ve agreed to be
2 responsible for Equaphor s legal fees?

3 A That is correct.

4 Q And they ve indicated they ve got an agreement with
5 or an understanding with Stein Sperling that Stein Sperling
6 will charge them little or nothing for representing Equaphor
7 along with or in addition to the representation of Kobayashi
8 and Dechman; correct?

9 A Yes.

10 Q Did you inquire why Stein Sperling was willing to
11 do that?

12 A Well, Stein Sperling -

13 Q You can answer that yes or no. Did you inquire?

14 A I don t think I inquired; no.

15 Q Have you discussed the issue of possible conflict
16 of interest with any attorney at Stein Sperling?

17 A As to that - I mean, back when I was looking into
18 whether Stein Sperling could pursue the litigation or not,
19 before this deal materialized, I think I looked into whether
20 or not a special counsel could be owed money or not by the
21 estate. I looked up some case law on that. I was looking
22 into conflict of interest at least in terms of what would
23 disqualify from the standpoint of the Bankruptcy Code; but
24 again, that was before the deal.

25 If you re asking whether I talked to somebody about

1

2 conflict of interest, per se, involving Stein Sperling
3 representing the estate in objecting to the claim of Carotex,
4 the answer is no.

5 **Q So, you did not have any discussion with a Stein**
6 **Sperling attorney about the conflict of interest question?**

7 A Did not.

8 **Q Do you have any of the pleadings? Did you get any**
9 **of the pleadings in the Carotex litigation?**

10 A Well, they re in the exhibit book that Mr. -

11 **Q Right. But before you entered into this agreement,**
12 **had you seen any of the pleadings in the Carotex litigation?**

13 A No.

14 **Q Did you know what the basis of the damage claim was**
15 **against Equaphor?**

16 A I had an understanding about that because I talked
17 to Mr. Adams in the courthouse one day about what was the -
18 you know, how could Carotex which said these patents were
19 worthless - how could Carotex have affirmative claims
20 against the debtor?

21 **Q What did you learn about the basis for the claims**
22 **against Equaphor?**

23 A He mentioned letters that were written by the
24 attorney for Equaphor, by Stein Sperling, and he
25 characterized them as letters to customers of Carotex,

1 asserting that there was a patent and they might be
2 infringing upon the patent and said that the business
3 stopped; the business with those customers froze up after
4 those letters were sent.

5 Q And he said it was sent by Equaphor s counsel,
6 Stein Sperling?

7 A Sent by Stein Sperling. Whether or not they were
8 representing Equaphor at the time, you know - hmmm.

9 Q Do you understand when the letters were sent?

10 A It was a couple of years ago.

11 Q Before Equaphor acquired the patents. If you
12 could turn to tab six in the exhibit book that Mr. Misken put
13 together. First, let s turn to tab six, if you would. I m
14 sorry. Never mind.

15 If you ll look at page CAR156 in tab six of Mr.
16 Misken s exhibit book, and you ll see a letter -

17 A Yes.

18 Q - on the letterhead of Stein Sperling, dated
19 November 26, 2007?

20 A Yes.

21 MR. SHAPIRO: I m sorry. Could I have just a
22 moment, Your Honor?

23 THE COURT: Yes.

24 MR. SHAPIRO: I apologize, Your Honor. This is not
25 the letter I was thinking of.

1 BY MR. SHAPIRO:

2 Q Well, it s your understanding, sir, that the
3 damage claim against Equaphor was based upon letters that
4 Stein Sperling had sent to customers?

5 A Yes.

6 Q And is it your belief those letters were sent on
7 behalf of Equaphor?

8 A Well, I find myself wondering how could Carotex
9 have a claim against Equaphor if the letters were sent before
10 Equaphor acquired the patents; but somehow, I have that
11 understanding.

12 Q Well, if you look at tab eight of the exhibit book,
13 there s a letter on Stein Sperling letterhead, dated April
14 24, 2008, addressed to a vice president of a company called
15 Pulp and Paper.

16 A I m sorry. Where are you?

17 Q Tab eight.

18 A Eight. Yes. I have seen a letter like this.

19 Q When did you first see it?

20 A Well, I think I saw it since our last get-together
21 in court here.

22 Q You saw it here in this book?

23 A No. I was actually sent a copy by Mr. Dechman but
24 the copy I was sent, because it was dated, you know, like
25 April 28

th of 2011, because the way Word operates, I
m sure

th of 2011, because the way Word operates, I

1 somebody just printed out a current version of it and Word
2 won t let you print it out with the original date on it.

3 **Q But Mr. Dechman sent you a copy of this letter**
4 **which is tab eight in the exhibit book?**

5 A A letter just like this but whether it was to this
6 particular customer or not, I don t know; and now I can
7 answer your question. Yes, the letter was sent on behalf of
8 Kobayashi.

9 **Q It begins, this -**

10 MR. SHAPIRO: Well, may I offer this into evidence,
11 Your Honor?

12 MR. MCCARTHY: I don t have any objection, Your
13 Honor.

14 THE COURT: It will be admitted.

15 (Carotex Exhibit No. 8
16 was received in evidence.)

17 MR. SHAPIRO: Is that D, Your Honor?

18 THE COURT: What?

19 MR. SHAPIRO: Is that D?

20 THE COURT: Well, it has been marked as Exhibit 8.

21 MR. SHAPIRO: I m sorry. Excuse me. Of course.

22 BY MR. SHAPIRO:

23 **Q And the letter begins, This law firm represents**
24 **Kobayashi Ventures which is the owner of certain patents,**
25 **et cetera; right?**

1 A Yes.

2 Q Do you understand then that the claim against
3 Equaphor is based upon letters that Kobayashi s law firm,
4 Stein Sperling, sent to customers of Carotex while Kobayashi
5 owned the patents?

6 A Yeah.

7 Q If you d turn to tab three in the exhibit book.

8 MR. SHAPIRO: I don t believe this has been
9 introduced into evidence, Your Honor. I would offer it into
10 evidence for not the truth of what s in it but for the
11 allegations. This is a copy of the document that was filed
12 in the Southern District of New York.

13 THE COURT: It will be admitted for that purpose.

14 (Carotex Exhibit No. 3
15 was received in evidence.)

16 BY MR. SHAPIRO:

17 Q It s tab three in the exhibit book, Mr. McCarthy.

18 A I see it.

19 Q Okay. Did you see this document before you entered
20 into the agreement, proposed agreement?

21 A No.

22 Q If you d look at page four of Exhibit 3. It s with
23 the Bates number CAR20-7.

24 A Yes.

25 Q And I direct your attention to paragraph 12 which

1 **alleges Upon information and belief, Defendant Dechman was**
2 **and is the moving, active, conscious force behind the**
3 **activities of Kobayashi and Equaphor that have damaged**
4 **Carotex and ECS business as complained of herein.**

5 MR. REYNOLDS: Your Honor, if I may objection. Mr.
6 McCarthy has already testified that he hasn t seen this
7 document before. I think the scope of the examination needs
8 to be: What did Mr. McCarthy review prior to accepting the
9 settlement? I think we are now going beyond the scope of
10 what that examination should be and -

11 THE COURT: I think he can say that had Mr. McCarthy
12 reviewed it, he would have seen this allegation and it might
13 have affected or might not have affected his determination
14 whether or not to settle. I ll overrule the objection.

15 THE WITNESS: I see that.

16 MR. SHAPIRO: Your Honor, I can shorten this a
17 little bit. I ll just call the court s attention to
18 paragraph 13 which alleges on information and belief that
19 Defendant Dechman personally authorized and approved the
20 activities of Kobayashi and Equaphor and that it damaged
21 Carotex and ECS business as complained of herein and
22 paragraph 17

23 MR. REYNOLDS: Your Honor -

24 MR. SHAPIRO: I won t read it but I ll just call
25 the court s attention to it.

1 MR. REYNOLDS: - these aren t questions.

2 MR. SHAPIRO: I m calling the court s attention to
3 something.

4 MR. REYNOLDS: But Your Honor, this has only been
5 admitted into evidence for the purpose of showing that this
6 is the second amended declaratory judgment filed up in New
7 York.

8 THE COURT: You can refer to it in argument. Let s
9 go on with the examination.

10 MR. SHAPIRO: Thank you, Your Honor.

11 BY MR. SHAPIRO:

12 Q Did you explore the possibility of reaching a
13 settlement with Carotex, that Equaphor would give up its
14 claims against Carotex if Carotex would release its claims
15 against Equaphor?

16 A Prior to making the deal that I made, I don t think
17 so. There have been some discussions since our last hearing.

18 Q Now, I understand your testimony from last week
19 that you were told by Mr. Dechman that the justification for
20 the sale of assets to Monitoring Technology and the sale of
21 the patents by Kobayashi to Equaphor were related to the sale
22 incentive fee? Do you recall that testimony?

23 A Yes.

24 Q Have you seen the sale incentive fee provision in
25 writing?

1 A Yes.

2 Q And where did you see it?

3 A I saw it attached to your opposition. It was -

4 Q Did you see it -

5 A Go ahead.

6 Q Go ahead. I m sorry. Go ahead.

7 A I ve seen it since our last hearing. I saw it
8 attached to your opposition and it was characterized to me
9 when I had spoke with Mr. Dechman and Mr. Fiore in our
10 lengthy meeting on Friday.

11 Q You did not see the actual document before you
12 entered into this proposed agreement?

13 A As far as I could tell, I saw the asset purchase
14 agreement but I didn t see the MSA that contained the sale
15 incentive fee. I saw the 09 agreement but not the actual
16 07 agreement, Your Honor.

17 MR. SHAPIRO: I would like to offer the Managements
18 Services Agreement, Your Honor, if there is no objection.

19 THE COURT: We will mark it as Bamber Exhibit D.

20 (Bamber Exhibit D
21 was marked for identification.)

22 MR. REYNOLDS: Your Honor, he may be able to get
23 this in through another witness but I think Mr. McCarthy has
24 testified that he hasn t seen it.

25 THE COURT: Well, he can show it to Mr. McCarthy and

1 ask him if he has seen it.

2 THE WITNESS: Well, this is what - oh, is there a
3 question?

4 BY MR. SHAPIRO:

5 Q This is what you ve seen in -

6 A This is what I ve seen that I was referring to
7 earlier; and I don t doubt that this is it, and I don t
8 object to its admission.

9 Q And this is dated in October of 2007 or actually
10 handwriting - that may be a different month. But it was
11 entered into in 2007, is your understanding?

12 A Yes.

13 Q All right. And I would ask you to turn to para-
14 graph eleven on page four.

15 A Yes.

16 Q Entitled, Compensation to Soze for sale of MTC?

17 A Yes.

18 MR. SHAPIRO: Your Honor, I don t know if there will
19 be an objection but if I could just explain some of the
20 nomenclatures so Your Honor is not totally lost here.

21 THE COURT: No. Examination is examination. I ve
22 told lawyers many times, don t interrupt it and explain to me
23 what s going on. You re not the witness. That s the
24 witness.

25 BY MR. SHAPIRO:

1 Q Were you aware that the company which is now named
2 Equaphor was previously named Monitoring Technology
3 Corporation or MTC?

4 A Yes.

5 Q And that when Mr. Dechman and Mr. Fiore bought the
6 assets, the remaining assets, business assets after the sale
7 to Cognex, that they took the name MTC or Monitoring
8 Technology and gave Monitoring Technology the new name,
9 Equaphor? Were you aware of that?

10 A Yes.

11 Q And what is now known as Monitoring Technology was
12 originally known as - I m not sure I know how to pronounce
13 it but S-o-z-e. Correct?

14 A I m aware of that.

15 Q And you re aware that Soze was an entity that was
16 created by Mr. Dechman and Mr. Fiore; correct?

17 A Yes.

18 Q So, paragraph eleven begins, In the event of a
19 sale, and it goes on to describe a formula for calculating
20 what s known as a sale incentive fee; correct?

21 A Yes.

22 Q And if you turn over to page five - I m sorry. Go
23 back to page four. In the first line of paragraph eleven it
24 says, In the event of a Sale, and you see Sale has a
25 capital S?

1 A Yes.

2 Q And then it says, parentheses, as defined below.

3 Correct?

4 A Yes.

5 Q And then turning over to page five, further down in
6 paragraph eleven - I m sorry. Okay. About four lines from
7 the end of paragraph eleven, do you see the sentence that
8 reads, Sale shall mean the sale of all or substantially all
9 of MTC s properties and assets to any person or entity. ?

10 A Yes.

11 Q And it s person or entity in the same - correct?

12 And you would agree that the sale to Cognex was not a sale of
13 all or substantially all of the assets of MTC; wouldn t you?

14 A Yes.

15 MR. SHAPIRO: I have no other questions, Your Honor.

16 THE COURT: I have only one question, Mr. McCarthy.

17 Under the asset purchase agreement, it s providing that the
18 sale of the patents would be free and clear of all licenses
19 which I assume would include the license to Carotex. The
20 question I have is, is that the intent and if so what is the
21 legal authority to sell free and clear of Section 365(N)
22 rights?

23 THE WITNESS: I don t think that was the intent.

24 For example, there are three paid-up licenses; and I think I
25 said in my opening statement that if the court does approve

1 the deal that I m going to submit a revised order to the
2 court that clarifies. Honeywell is in there and PaperTech is
3 in there. I don t think there was any intent to prejudice
4 any license rights.

5 Now, you know, there s so much in there about we
6 have the right to pursue, you know, the litigation against
7 Carotex; but I don t know that it occurred to anybody that,
8 you know, we were undermining that by saying, free and clear
9 of any licenses that Carotex might have because that s kind
10 of part and parcel of the litigation.

11 THE COURT: Well, I guess that was the question,
12 whether that was an attempt to in effect short-circuit the
13 litigation by pulling the rug out under Carotex.

14 THE WITNESS: That would not be my understanding.

15 THE COURT: Okay.

16 MR. McCARTHY: Your Honor, could I do some redirect
17 of myself?

18 THE COURT: Yes, you may.

19 REDIRECT TESTIMONY

20 MR. McCARTHY: There have been many questions about
21 what did I review, and I would like to offer this into
22 evidence.

23 THE COURT: The court security officer will take it.
24 We ll mark it.

25 MR. McCARTHY: Well, I actually marked it. I guess

1 we need to call it Trustee s Exhibit A.

2 THE COURT: Right. We will call it Trustee s
3 Exhibit A.

4 (Trustee s Exhibit A
5 was marked for identification.)

6 MR. McCARTHY: What this is is simply covering e-
7 mails that I assembled over the weekend to refresh myself on
8 what all I had looked at, and that s why I developed the
9 Redweld I mentioned earlier. I actually have the documents
10 here in Redweld.

11 So, I looked at everything that is mentioned here,
12 Equaphor payables during the last 90 days; the Whiteford
13 invoice; Aronson invoice; some Cognex invoices, as well;
14 Kobayashi, LeClair Ryan, Lindeman and Stein Sperling
15 invoices. I looked at the promissory note that Kobayashi
16 took back from the debtor after the 09 agreement for
17 \$500,000 and the two balance sheets - remember I mentioned
18 10/31/09 and 9/26/09. Those were attachments to this
19 February 15

th e-mail from Steve Ramsdell.

20 There are additional documents he also sent me on
21 February 15

th. This is mostly the transfers.

There was a
22 spreadsheet that had who got what and when during the year
23 prior to the bankruptcy. This is what I looked at when I was
24 going through whether I thought there was a solid preference
25 claim or not against different entities; and I went through

1 that on the phone with - and I think Mr. Dechman and Molly
2 Hale, the controller, may have been in on that conversation,
3 at least on the conversation or he was talking to her while I
4 was talking to him.

5 And then the bylaws, and I looked at the bylaws on
6 March 9th. This is from Dechman to me, telling me where to
7 look for the indemnification provisions, and I did look at
8 those. That formed the basis of my understanding.

9 Also, the question has been raised about the
10 Carotex claim. The court can take judicial notice. There s
11 a four-million-dollar claim filed by Carotex on Friday, the
12 29th; also one filed by ECS. I kind of think they re the same
13 thing. I don t know if they meant eight million or four
14 million; but whatever, they are big claims.

15 I have received snippets of skepticism towards
16 Carotex s claims against the debtor in conversations with
17 both Mr. Dechman and a conversation I had with Jeff Schwaber,
18 the main litigation counsel for Equaphor in the Carotex
19 suits.

20 Over the weekend, Mr. Dechman sent to me - and I
21 have it in my bag but it s a transcript of a hearing from the
22 District Court in which - I think it s a partial summary
23 judgment ruling, you know, and I just looked very quickly at
24 it. Mr. Dechman sent me an e-mail, an excerpt from it in
25 which the judge said something like: Writing letters and

1 asserting that there is a patent infringement as a basis for
2 a claim against the writer of the letter is kind of something
3 new, beyond ordinary patent misuse litigation. She seemed
4 very skeptical of the claim; and I would say, you know, I
5 didn't have that in my head when I made this deal but there
6 were questions raised about Carotex's claims against the
7 debtor.

8 I remember wondering, gee, is writing - I mean,
9 you know, in other areas of the law, if you think you have a
10 claim you have a right to assert it without necessarily
11 triggering a tort. I remember thinking that that might not
12 be a good claim. But what do I know? And then, you know,
13 that's just my intuitive general lawyer sense, plus Mr.
14 Schwaber having expressed some skepticism about Carotex's
15 position overall and then this Federal District judge saying
16 the same kind of thing makes me think those aren't good
17 claims, at least on the merits.

18 So, that concludes my redirect.

19 MR. SHAPIRO: I have a couple of follow-up
20 questions, if I may, Your Honor.

21 THE COURT: Certainly.

22 MR. MCCARTHY: Could I move this into evidence, Your
23 Honor?

24 THE COURT: I'll admit Trustee's Exhibit A.

25 (Trustee's Exhibit A

1 was received in evidence.)

2 RECROSS EXAMINATION

3 BY MR. SHAPIRO:

4 Q First, just one or two questions about Exhibit A
5 or Trustee s Exhibit A. In the second e-mail on the first
6 page, the February 1, 2011 e-mail, and the fourth line, it
7 refers to I also understand that principals of my client
8 will be in touch with you through Jim Reynolds. Did you
9 understand that to refer to Mr. Dechman and Mr. Fiore as
10 principals of Equaphor?

11 A I m sorry. Where are you?

12 Q The fourth line in the February 1 e-mail, on the
13 first page of Trustee s Exhibit A. There s an e-mail from
14 Mr. Ramsdell who is bankruptcy counsel for Equaphor; correct?

15 A Yes.

16 Q And it refers to principals of my client will be
17 in touch with you through Jim Reynolds. Is it your
18 understanding he was referring to Mr. Dechman and Mr. Fiore
19 as the principals?

20 A Oh, yes.

21 Q And then on the next page, Mr. Ramsdell gives
22 contact information for Molly Hale, controller, Monitoring
23 Technology?

24 A Yes.

25 Q And you re aware that Molly Hale is an employee of

1 **Mr. Dechman and Mr. Fiore at Monitoring Technology?**

2 A Yes. I am.

3 Q And you are aware that she was one of the directors
4 who voted to put the company into bankruptcy?

5 A Yes.

6 Q And she was one of the directors who voted in
7 favor of the asset purchase agreement with what was then
8 Soze, what is now Monitoring Technology, and the patent
9 purchase agreement between Kobayashi and Equaphor?

10 A Yes.

11 Q Do you have the bylaws with you that you examined?

12 A I do.

13 MR. SHAPIRO: May I see them, Your Honor?

14 THE COURT: After Mr. McCarthy locates them.

15 THE WITNESS: I have them here. It has a work
16 product note on it but I don t mind exposing that to the
17 court.

18 (Document handed to Mr. Shapiro.)

19 MR. SHAPIRO: If I could have just a moment, Your
20 Honor.

21 THE WITNESS: I think I may have marked the
22 pertinent part there, Mr. Shapiro, with a post-it.

23 MR. SHAPIRO: Thank you.

24 (Pause.)

25 MR. SHAPIRO: I would like to offer this into

1 evidence, Your Honor.

2 MR. McCARTHY: No objection.

3 MR. REYNOLDS: No objection.

4 THE COURT: We will mark it as Bamber s Exhibit E.

5 (Bamber s Exhibit E

6 was marked for identification.)

7 BY MR. SHAPIRO:

8 Q The work product note, is that just the note on
9 the first page or are there other notes in here?

10 A No. That s it.

11 MR. SHAPIRO: Okay. Thank you. I have no other
12 questions.

13 THE COURT: We ll put it on the witness stand but
14 don t run away with it, Mr. McCarthy; but we will make a copy
15 for you after the hearing. Anything further? Thank you for
16 testifying. You may stand down.

17 MR. McCARTHY: Thank you, Your Honor.

18 Your Honor, shall I leave all of the exhibits?

19 THE COURT: All of the exhibits there. Yes, please.

20 Did you have any witnesses you wish to call, Mr.
21 McCarthy?

22 MR. McCARTHY: I do, Your Honor. I would like to
23 call Mr. Dechman and also one of the directors, Mr. Doherty.

24 THE COURT: Okay. Mr. Dechman, if you will please
25 stand in front of the clerk and be sworn.

1 Whereupon,

2 JAMES DECHMAN

3 was called as a witness and, having been first duly sworn,

4 was examined and testified as follows:

5 DIRECT EXAMINATION

6 BY MR. MCCARTHY:

7 Q Mr. Dechman, would you state your name and address,
8 please?

9 A James Dechman, 3189 Mary Etta Lane, Oak Hill,
10 Virginia.

11 Q What is your position with Equaphor?

12 A President and CEO.

13 Q And what is your position with Kobayashi?

14 A Managing member.

15 Q And what is your position with Monitoring
16 Technology, LLC?

17 A Managing member.

18 Q Could you please describe for the court the 2007
19 transactions between Equaphor and Monitoring Technology, LLC?

20 A In 2007, there were three transactions. The first
21 was a Management Services Agreement between Equaphor and
22 Monitoring Technology, LLC; and there was a patent waiver
23 agreement between Equaphor and Kobayashi Ventures, and there
24 were purchases of F shares from individual shareholders by
25 Monitoring Technology, LLC.

1 Q Would you tell the court how the debtor or how you
2 paid the debtor for the patent waiver and, you know, the
3 other transactions? How did the money go back and forth and
4 what were the terms going on in that connection?

5 A Again, this was in 2007. Just a quick backdrop.
6 There were three board members, J.B. Doherty, Ed Spiva and
7 John Evans, and the three of them represented venture capital
8 firms that owned 76 percent of Equaphor. They had made their
9 investments at least back in 1996. So, they had been
10 involved with the company for the last eleven years in a
11 controlling situation on the board.

12 And in 2007, we had just finished a lawsuit with a
13 company called ABB and -

14 THE COURT: Called what?

15 THE WITNESS: Sorry. ABB.

16 THE COURT: ABB. Okay.

17 THE WITNESS: ABB. And in that lawsuit - as a
18 result of a settlement in that lawsuit and as a result of a
19 compensation package that the board had approved for John
20 Fiore and myself back in - I think the compensation package
21 was put in place in 2004 and it continued.

22 So, as the basis of that compensation package, we
23 were due a bonus of two and a half million dollars at the end
24 of 2006; and so, the board in 2007 was negotiating to come up
25 with a structure where it could retain John Fiore and myself

1 to manage Equaphor and to help prepare for a sale of the
2 company.

3 So, with the details of the Management Services
4 Agreement was a three-year management contract at a million
5 dollars a year that John Fiore and myself would share and a
6 sales incentive fee, that if we were able to sell the company
7 we would be compensated at a - for a sales commission over
8 the investor premium plus the book value of the assets less
9 liabilities.

10 So, there s the sales commission fee and then the
11 patent waiver agreement. Equaphor was agreeing to allow
12 Kobayashi to pursue and try to acquire patents that
13 International Paper owned and that Equaphor had been a
14 licensee of, and Equaphor had accrued liability for those
15 patents, licensing fees. And Equaphor had a desire to try
16 to have the market be more level. Some competitors weren t
17 paying their license fees and some were.

18 And on the third piece, the share purchase piece,
19 they were working to try to get management to be aligned with
20 shareholders. So, for \$1.8 million we purchased individual
21 shares from individual F shareholders. As a result of
22 those purchases, Monitoring Technology, LLC ended up owning
23 43.5 percent of the Series F shares. So, roughly 88 percent
24 of the Series F shareholders agreed to sell their shares to
25 us for the 1.8 million.

1 Q What happened to the \$2.5 million in bonuses as
2 part of this?

3 A It was never paid; and so, it was kind of bundled
4 into these other agreements.

5 Q And what would happen if you hadn t been able to
6 sell any of its services agreement - what would happen if
7 you weren t able to sell the business in three years?

8 A Right. So, yeah. It s another provision in the
9 MSA. If we were unable to sell within the three years, we
10 had to manage Equaphor for free for years four and five. So,
11 I mean, the bottom line was a, you know, for the board - and
12 again, Mr. Doherty or Mr. Spiva can testify if needed on
13 that.

14 But I think the desire in 2007 was to retain
15 management, avoid the \$2.5 million of cash outflow which
16 would have put Equaphor in a difficult financial position
17 with no management and to have management invest in the
18 company and to encourage Kobayashi to purchase the patents
19 and try to level the playing field out in the market.

20 Q All right. Did you discuss all of this with me
21 prior to our entering into the deal that s before the court
22 now?

23 A Absolutely. Yes.

24 Q And do you recall what documents you provided to
25 me?

1 A Well, for the 2007 transactions, uh -

2 Q Well, let me withdraw that question. I ll withdraw
3 that question.

4 And was the board represented by counsel in 07
5 when these three agreements that you mentioned were entered
6 into?

7 A Yes. The negotiation for these agreements lasted
8 just over nine months. So, it took quite a bit of time;
9 and George Lawler of Whiteford Taylor represented Equaphor.

10 Q All right. And did you discuss that point with me
11 prior to our entering into the agreement?

12 A Yes.

13 Q And who all was on the board of directors at that
14 time?

15 A Mr. J.B. Doherty, Ed Spiva and John Evans.

16 Q And what was the vote in connection with the 07
17 agreements?

18 A It was unanimous support.

19 Q And were those directors independent of management
20 at that time?

21 A Yes.

22 Q Did you discuss that point with me prior to our
23 entering into the agreement?

24 A Yes.

25 Q Would you please describe for the court the 09

1 **transactions involving the debtor, Cognex and Monitoring**
2 **Technology, LLC?**

3 A Sure. So, in September and October of 2009, the
4 different agreements were a sale of Equaphor s Smart Advisor
5 video operating business to Cognex Corporation, a sale of
6 the Hindsight and Smart Advisor vibration operating business
7 to Monitoring Technology, LLC and a purchase by Equaphor of
8 patents that Kobayashi Ventures owned.

9 **Q And how did the money go back and forth in**
10 **connection with those deals?**

11 A The Cognex agreement was for \$5 million for the
12 Smart Advisor video operating business, some inventory, work
13 in process parts, and that was for \$5 million; 4.5 million
14 paid up front and 500,000 to be held in escrow for 12 months.

15 The purchase by Monitoring Technology, LLC was for
16 1.5 or 1.6 million for the Hindsight video business and Smart
17 Advisor vibration business, for remaining accounts
18 receivables, remaining inventory, remaining accounts payables
19 and remaining service contract liabilities. I m sure I m
20 leaving off some assets and liabilities.

21 And then the patent purchase was for \$3.45 million,
22 2.95 million to be paid in cash and 500,000 to be paid in the
23 form of a note that was due in three years.

24 **Q And what role, if any, did a non-compete agreement**
25 **play in connection with the Cognex transaction?**

1 A Exactly. So, you know, again in - so, in 2009,
2 there were five directors on the board; and so, again, Mr.
3 Doherty and Mr. Spiva, Mr. Evans were still on the board -
4 MR. SHAPIRO: Objection, Judge. Non-responsive.
5 The question was about a non-compete.

6 THE COURT: I think he s trying to lay the
7 background for it. I ll overrule the objection.

8 BY MR. McCARTHY:

9 **Q Continue.**

10 A Okay. So, there were five directors. So, Mr.
11 Doherty, Mr. Spiva, Mr. Evans and Miss Hale and Mr. Sumner
12 Kaufman were on the board; and obviously, the three directors
13 that originally entered into the Management Services
14 Agreement were still on the board and still in control at
15 that point.

16 As has been talked about here, the Management
17 Services Agreement has language in it that deals with a
18 sales incentive fee and a requirement to sell the company if
19 the company sells substantially all of its assets.

20 So, leading up to this, the events in 09 - in
21 September 09 the board had been meeting for about nine
22 months, reviewing different proposed deals and updates on
23 Cognex and doing some pretty detailed minutes on how
24 different deals would work and how they would fit with the
25 MSA and even spreadsheets and models showing how money would

1 be handed to the - or available to the shareholders for
2 dividends.

3 So, there was a whole structure in place using the
4 MSA of what - what the sales incentive fee payment would be
5 and what the - remaining payments due and the Management
6 Services Agreement.

7 So, I m getting back to the non-compete because
8 what ended up happening is, the deal always happens a little
9 different than you expect and Cognex required a pretty
10 substantial non-compete from John Fiore and myself, a
11 personal non-compete for five years and \$250,000 per incident
12 personally, separate from any non-compete required by
13 Equaphor.

14 THE COURT: I m sorry. I missed what the 250,000
15 was for.

16 THE WITNESS: Sure. Cognex - and Cognex is a
17 billion-dollar company. They re not as big as General
18 Electric but they re fairly big. Their CEO and founder
19 actually got involved in this non-compete requirement and he
20 actually wrote the language for it and it requires John Fiore
21 and I to pledge \$250,000 personally per incident if we were
22 to compete with the provision that again he wrote and there s
23 language about what businesses were not allowed to
24 participate in or compete with Cognex in.

25 And Equaphor has a non-compete provision, too, as

1 the company, but they wanted it specifically from John Fiore
2 and myself, as well.

3 Prior to these deals, there were no agreements
4 between us and Equaphor or the board to not compete in a
5 certain area for five years. So, it was a new requirement.

6 And so, when we were involved in the September
7 negotiations, we ended up doing a deal that used the
8 Management Services Agreement as some framework but we ended
9 up restructuring the deal to have Equaphor purchase the
10 patents from Kobayashi; and by paying 3.45 million for the
11 patents, it - Monitoring Technology, LLC would waive some of
12 the fees that were due in the MSA.

13 So, for the board, they could have stayed more with
14 the MSA, more consistent with the minutes that they had
15 worked on over the summer and if they had done that they
16 would have paid a million dollars for the third year for the
17 management service contract. They would have paid \$900,000
18 for the - 950,000 I think it was for the licensing fee to
19 Kobayashi and they would have paid a million and a half for
20 the sales commission fee based on the calculation which
21 ended up totaling 3.45 million.

22 So, instead of going that route, they accepted a
23 deal where they would purchase the patents for the same
24 amount and get to keep 500,000 in the company to help give
25 the company money to enforce the patents and keep upside if

1 they were able to successfully enforce the patents and get
2 these non-competes from John Fiore and myself, as well.

3 Q And did you discuss all of that with me prior to
4 entering into our compromise and sales agreement?

5 A Yes.

6 Q And what was the reason for the timing of the 09
7 transactions?

8 A Yes. Cognex was a friendly party in the
9 transactions but they were a little scary because they were
10 big. So, we had started talking to Cognex about a year
11 before and made good progress for a couple of months and they
12 were looking at buying the whole company at that point and
13 then kind of after three months they just went totally silent
14 and couldn't understand what was going on.

15 Then they came back and said that they weren't
16 interested. So, then things settled for a couple of months
17 and then we went back and talked to them again about just
18 selling the Smart Advisor video portion and they seemed
19 interested again and so we started working through that deal.

20 Again, you know, the board is controlled by venture
21 capitalists. So, we had board minutes and the board approved
22 for John Fiore and I to have discussions with Cognex and we
23 were continuing to work with them and they had told us near
24 the end of this deal that it was time to either get the deal
25 done or not and that they had a big trade show coming up and

1 they had a competitor that had a product that was - they
2 were buying our product to integrate it with one of their
3 products so that they had an integrated solution in the
4 market and one of their competitors had a similar product
5 already.

6 They were putting a lot of pressure on us to get
7 the deal done. They knew we had a board meeting coming up
8 and they expected to get closure on the deal from our side.
9 And so, they were putting quite a bit of time pressure and
10 they were basically threatening to - that they could do a
11 deal with somebody else similar to us that had a similar
12 product that they could integrate. So, we were pushing hard
13 to close the deal and get it done.

14 **Q Now, it ended up that Equaphor ended up paying**
15 **apparently 800-and-some thousand dollars of attorney fees,**
16 **0-10?**

17 A 2010. Yes.

18 **Q When the deal was made in 09 whereby the patents**
19 **were acquired by Equaphor, what was the expectation of how**
20 **the litigation with Carotex would play out at that time?**

21 A Well, I mean, that s a - it s a great question.
22 I mean, again, Carotex - you know, Carotex entered into a
23 licensing agreement on these patents in I think it was 2000
24 or 1999 and had made some payments and then had stopped
25 making payments, and they had filed suit against Kobayashi

1 in a declaratory judgment and their initial claim was that
2 PaperTech, another company in this market, was not paying
3 anything and therefore Carotex shouldn't have to pay
4 anything.

5 And so, our hope around the timing of the
6 September, October, '09 transactions was that PaperTech was
7 getting very close to a settlement and we thought, gee, if we
8 could get PaperTech to settle then maybe Carotex would
9 settle, and if we could get both of them to settle then we
10 could use some money to go after the other four or five
11 competitors in the market.

12 It's not a huge market but there's, you know, five
13 or six players in the market that were all using - we
14 believed using the technology and the patents and not paying
15 royalties.

16 So, we thought if we could get PaperTech to fall
17 then Carotex would do an agreement along - again, we already
18 had Honeywell and Cognex ended up getting a license, too, as
19 part of their deal. So, that had been our hope.

20 And so, we left 500,000 in Equaphor. We were
21 hoping that would be enough seed money to steer through that;
22 and as it turned out, that was not the case. As you
23 mentioned, the legal fees were gigantic and there's this
24 whole - and again, I'm a mechanical engineer. So, I don't
25 follow a lot of the patent stuff but it's a - the Markman

1 hearing on these patents is a complicated and very expensive
2 proposition.

3 What happened in 2010 is that after a couple of
4 years of kind of start-and-stop litigation with Carotex in
5 New York, the court got focused and got everybody on a
6 Markman schedule; and you know, when you re on that schedule,
7 it drives a certain level of costs.

8 So, out of the 800,000 spent in 2010, I - I mean,
9 some of the money was clearly - you know, the derivative
10 suit was filed in the summer of 2010; and again, Equaphor had
11 counsel and they reviewed the derivative suit and directors
12 and officers submitted personal agreements where we pledged
13 to pay back any money if the indemnification claims were
14 deemed invalid later.

15 At that time, Equaphor could - and again, based on
16 the board vote, Equaphor began to reimburse legal fees
17 related to the derivative suit, too. So, of that 800,000 I
18 would guess - you know, I mean certainly some portion was
19 used for defending the directors and officers in that suit.

20 **Q With respect to Cognex pressuring you to get a**
21 **deal done, is that something that you discussed with me prior**
22 **to our own agreement?**

23 **A Yes.**

24 **Q After the money came into the company from the**
25 **Cognex deal was there a liquidating dividend out to the**

1 **Series F shareholders at that time?**

2 A Yes. Exactly. Very soon after the deal. I think
3 within a week, the board - again, and I left that off there.
4 So, just stepping back briefly, on the deals that were done
5 in September, October, there were five directors. Three were
6 the original venture capital directors. One was Molly Hale
7 and one was Sumner Kaufman. Of those voting, three voted for
8
9 and Mr. Evans abstained and Mr. Kaufman voted against.

10 The liquidating dividend, the 5.2-million-dollar
11 liquidating dividend that was then approved - actually it
12 was unanimously approved by everyone on the board and it was
13 paid out just following the transactions in early October.

14 **Q What were conditions like in Equaphor s industry**
15 **when the 09 transactions were approved?**

16 A I mean, that was a dark time in the industrial
17 market. So, you know, to go back in perspective, you know,
18 industrial customers were our customers. You typically work
19 off of a backlog; and so, you know, somebody in a factory
20 buys some equipment and they have to get capital approved and
21 then they have to go through a process to actually spend that
22 capital and the manufacturer takes time to produce. I mean,
23 you re not selling shampoo. You re actually selling, you
24 know, a large capital asset. And so, you work off a backlog.
25 With the financial meltdown factories started to

1 not spend; and so, we saw revenues - we saw orders - excuse
2 me - orders drop significantly over the 12-month period. We
3 were happy to be able to get a deal done during those times.

4 Q All right. Had you been able to sell the company
5 for more or to a third party for more than what you ended up
6 selling the various parts of the company for under these
7 deals you ve described in 09? Under the MSA, how would that
8 have been affected?

9 A Exactly. So, again, a lot has been talked about in
10 this sales incentive fee and whether it was capped or how it
11 actually worked. The way that fee worked is that - the key
12 piece in there or one of the key pieces in there is the
13 investor s premium and investor s premium was based on a
14 multiple of free cashflow, basically the net income of the
15 enterprise for the prior 12-month period.

16 And so, if the company kept growing a lot and
17 making a lot of profit then the investor premium would keep
18 getting higher over time.

19 The sales incentive fee was capped on the specific
20 day, basically, that the deal was done because it looked at
21 the free cashflow for the 12 months prior and calculated the
22 investor premium.

23 So, you know, on the time that the transaction
24 actually occurred with Cognex, if somebody else had offered
25 substantially more money then the free cashflow would have

1 still been the same and the investor premium would have still
2 been the same. And so, the sales commission fee would have
3 gotten bigger, dollar per dollar, of anybody else paying
4 anything more; and all of this had been reviewed quite a bit
5 in board minutes with spreadsheets and models.

6 It was pretty clear to all the directors of how
7 this work; and again, the three - I guess my bottom-line
8 point is, the three venture capitalists that had all been
9 invested in the company since 1996 and approved the MSA, who
10 were 76-percent shareholders and controlled the board at all
11 times, they all agreed to all of these deals. They were all
12 in writing and they still agree with all these deals. So,
13 they understood.

14 So, stepping back again, if the deal was for more
15 money, it would have just increase the sales incentive fee.

16 **Q All right. Did you discuss that point with me**
17 **priori to our agreement?**

18 A Yes.

19 **Q Okay. Who owned the majority of Series F stock**
20 **back in 07?**

21 A Prior to Monitoring Technology purchasing 43.5
22 percent, the three venture capital groups owned together
23 76 percent of Series F and Series E actually.

24 **Q What did they end up doing with their stock?**

25 A In the fall of 2007, they sold just under half of

1 their holdings to Monitoring Technology, LLC along with I
2 think another ten or 15 investors sold a part of their
3 holdings to Monitoring Technology, LLC, and then they kept
4 their remaining shares. So, they sold off just under half of
5 their shares in 2007 to Monitoring Technology, LLC.

6 **Q What about in 09?**

7 A And in 09, they still had their shares, same
8 number of shares. So, at that point, they would have had
9 39 percent of the company. So, in 09, they would have had
10 39 percent of F. Monitoring Technology, LLC would have
11 had 43.5 percent and then the other, you know, 18 percent
12 would be the other shareholders.

13 **Q Did they sell shares after 09?**

14 A They did. They held their shares for the 5.2-
15 million-dollar distribution and then they received - they
16 received their money along with all the other shareholders.
17 It went through the liquidation dividend and then the three
18 V-Cs sold their remaining shares to us beginning in December
19 2009 and through I think around May 2010.

20 **Q All right. And if the court approves this deal,**
21 **how will the Series F shareholders who didn t sell to you**
22 **fare compared to those who did sell?**

23 A So, I mean, it s all pretty interesting. So, if
24 you - as the majority holders, when they sold their shares
25 to us in 07 for the \$1.8 million, that was actually lower

1 than what the company ended up selling for, if you follow my
2 point.

3 So, they - you know, those shareholders that sold
4 to Monitoring Technology, LLC in 2007 received 1.8 million
5 divided by the number of shares and the enterprise later on
6 ended up being worth, you know, as cashflow and dividends,
7 et cetera, around \$8 million. So, they, you know, sold their
8 piece of their shares for less than what it ended up selling
9 for.

10 So, as the bottom line, an F shareholder who
11 decided not to sell us their shares in 07 and who kept their
12 shares actually made more per share on their investment
13 than any of the majority shareholders because the majority
14 shareholders sold their shares in 07 for less money than
15 the company ended up being worth in 09.

16 Now, some of those F shareholders still have not
17 sold their shares. So, they still - there s 16.5 percent
18 that still own their F shares and we - as part of the
19 offer, we made an offer to purchase their remaining shares
20 for a hundred thousand which is 50 percent more than what
21 the, say, venture capitalists were paid for their remaining
22 shares, as an example. So, again, they would make more per
23 share than the venture capitalists made.

24 Q All right. Did you discuss that aspect of the
25 deal with me prior to our making the agreement?

1 A Yes.

2 MR. McCARTHY: Okay. I don t have any more
3 questions, Your Honor.

4 THE COURT: Okay.

5 CROSS EXAMINATION

6 BY MR. MISKEN:

7 Q Good afternoon, Mr. Dechman.

8 A Good afternoon.

9 Q At the time that the patents were sold to
10 Equaphor, you were a member of Kobayashi Ventures, LLC;
11 correct?

12 A Yes.

13 Q And I believe you testified you were the managing
14 member?

15 A Yes.

16 Q And who were the other members of Kobayashi
17 Ventures at that time?

18 A Just John Fiore.

19 Q Did you guys have separate ownership percentages or
20 how was it broken out?

21 A We each owned half.

22 Q Has that ownership structure changed since the sale
23 of the patents to Equaphor?

24 A No.

25 Q And at the time the patents were sold to Equaphor,

1 **you were a member of Monitoring Technology, LLC?**

2 A Yes.

3 **Q And were you also the managing member of Monitoring**
4 **Technology?**

5 A LLC; yes.

6 **Q LLC. And who were the other members of Monitoring**
7 **Technology, LLC?**

8 A John Fiore and Steve Book.

9 **Q And what were your membership percentages?**

10 A What they currently are are I own 40 percent; John
11 Fiore owns 40 percent, and Steve Book owns 20 percent.

12 **Q And was that the same percentages at the time the**
13 **patents were sold to Equaphor?**

14 A I m not sure. Steve originally bought in for less
15 and then increased his share later. I m not sure about the
16 timing.

17 **Q Kobayashi has offered to purchase the Equaphor s**
18 **patents from the bankruptcy estate; correct?**

19 A Yes.

20 **Q And Kobayashi purchased the patents in October**
21 **2007?**

22 A On or about there from International Paper; yes.

23 **Q Did they buy it from International Paper or did**
24 **they purchase them from Jacklin Associates?**

25 A Right. Correct. Yes. They purchased them from

1 Jacklin Associates.

2 Q And Jacklin Associates was the entity that
3 purchased them from International Paper?

4 A Yes; and then Kobayashi had an agreement with
5 Jacklin for an immediate transfer to Kobayashi as part of
6 the purchase.

7 Q Were you a shareholder of Jacklin Associates?

8 A No.

9 Q Were you an officer in Jacklin Associates? Any
10 relationship with Jacklin Associates at all?

11 A No. No.

12 Q Any of the other members of Kobayashi have any
13 relationship with Jacklin Associates?

14 A No.

15 Q Jacklin Associates was formed for the expressed
16 purpose of acquiring the patents; is that correct?

17 A No.

18 Q So, why did Jacklin Associates acquire the patents
19 then?

20 A They were paid a - I think it was a 5,000-dollar
21 fee to help with the transaction. It might have been 10,000;
22 five or ten thousand.

23 Q Is it your position that Kobayashi could have
24 purchased the patents directly?

25 A From?

1 **Q From International Paper.**

2 A I m sure that they could have. I imagine. Yes.

3 **Q Why was this transaction set up to have Jacklin**
4 **Associates purchase the patents?**

5 A We were trying - International Paper was -
6 Equaphor had tried to purchase the patents or get a paid-up
7 licensing fee from International Paper several times over the
8 years; at least two or three times. We even hired one of the
9 ex-International-Paper employees to help broker a deal and
10 each time it had failed. And again, International Paper is a
11 gigantic company. So, it s a little hard to figure out
12 exactly why it failed but certainly being a licensee and
13 having that relationship made it more complicated and,
14 frankly, we were concerned about, you know, International
15 Paper focusing on Equaphor and requiring Equaphor to, you
16 know pay up on its royalties that it had been accruing.

17 And so, we thought it would be valuable to have an
18 intermediary company work to purchase the patents, and
19 International Paper was focused on some divestitures at the
20 time and it seemed interesting to have - you know, to kind
21 of go about it as just a patent purchase which ended up being
22 successful at the time. Of course, we didn t know it would
23 be successful but it ended up being good strategy.

24 **Q And then in I believe it was December 2007 or**
25 **October 2007 Kobayashi purchased the patents from Jacklin or**

1 **how did that transaction -**

2 A There was an agreement between Kobayashi and
3 Jacklin where Jacklin would attempt to purchase the patents
4 from International Paper and then the portfolio would be
5 transferred immediately to Kobayashi and Jacklin be paid a
6 finder s fee.

7 **Q How much did Jacklin purchase the patents for from**
8 **International Paper?**

9 A It was a long agreement and the immediate cashflow
10 was 75,000, to my memory, and then there was - what - what
11 International Paper wanted was to have someone buy the
12 patents and enforce them which it knew would be expensive to
13 enforce them but if the enforcement went well then
14 International Paper would share in the proceeds. They didn t
15 want to sell something and, you know, we ended up enforcing
16 and making a lot of money and then they would look funny.

17 So, the deal ended up being 75,000. I believe that
18 was the number up front and then 50 percent of the net
19 proceeds of whatever was collected and then there were
20 minimum payments each year regardless of what was collected
21 of I think 25,000, and I think those minimum payments - the
22 minimums I think added up to 125,000. I probably need to
23 look at the agreement before I go too far. But that was just
24 minimum. So, if we went out and collected \$2 million net
25 then they would be due their 50 percent of that net.

1 **Q How much was actually paid to International Paper**
2 **for those patents?**

3 A Well, at the time, it was 75,000 paid up front and
4 then - you know, for the first year - I guess two years.
5 That was October 07. So, yeah, for two years. We collected
6 some money and we spent a lot of money. So, it ended up not
7 being that great of an investment to start off with; and so,
8 IP just - they received their 75. I can't remember if we
9 paid them one minimum payment. But right around the timing
10 of one of the minimum payments, either the first one or the
11 second minimum, we had further conversations where we
12 negotiated to buy the patents outright from them, and then
13 that was payment of 150,000 in addition. So, I know we paid
14 225,000 and I believe that was it.

15 **Q And that was Kobayashi that made those payments;**
16 **correct?**

17 A Well, yeah. Again, as I said, Jacklin, you know,
18 paid the first 75 but then Kobayashi paid Jacklin. I believe
19 it was 80 or 85; and then Kobayashi paid the second 150
20 directly to IP.

21 **Q Did Kobayashi obtain any opinions regarding the**
22 **value of those patents at the time of the purchase?**

23 A No; but when we - Mr. Fiore and myself, when we
24 were at Equaphor, we had reviewed the patents because we were
25 licensees and, you know, everybody we reviewed them with said

1 that they looked good and obviously were worthy of trying to
2 purchase.

3 Q Was there any litigation, any pending litigation or
4 threatened litigation at the time Kobayashi purchased the
5 patents?

6 A From Jacklin? Not that I m aware of; no.

7 Q And then Kobayashi sold the patents to Equaphor in
8 September 2009; correct?

9 A Yes.

10 Q And who negotiated that sale on behalf of the
11 debtor?

12 A Well, you know, obviously the board. Ed Spiva was
13 the chairman of the board. He had the principal role but I d
14 say the other directors were obviously involved, as well.

15 Q You were not a member of the board of Equaphor at
16 this time?

17 A No. Actually, I - I - the last time I was on the
18
19 board of Equaphor was in early 07 and Mr. Fiore did get on
20 the board but it was in late 2010. So, for this period of
21 time either of us were on the board.

22 Q Were you an officer of Equaphor at that time?

23 A Yes.

24 Q And what was your position?

25 A President and CO.

1 **Q And how about Mr. Fiore? What was his position**
2 **with Equaphor at that time?**

3 A He was the chief technology officer. Again, at
4 that time, both of us were on contract through the Management
5 Services Agreement. So, we - you know, I mean to be
6 precise, Equaphor contracted with our services to fulfill
7 those roles through the Management Services Agreement.

8 **Q Well, did you or the debtor obtain any opinion from**
9 **a non-insider, third party as to the value of the patents at**
10 **the time that Equaphor purchased the patents?**

11 A No. As I said earlier, the value of the patents is
12 largely driven by the value of the payments that were due
13 from Equaphor to either Monitoring Technology, LLC or
14 Kobayashi Ventures for other services.

15 **Q At the time of the sale of the patents to the**
16 **debtor was there any pending or threatened litigation with**
17 **regard to the patents?**

18 A Yes. So, at the time of the sale, the PaperTech
19 case was still active and the Carotex and ECS cases were
20 active.

21 **Q That s the New York action that we ve been**
22 **referencing here; correct?**

23 A Yes; along with PaperTech which was also a New York
24 action.

25 **Q In that action, Carotex challenged the validity of**

1 **the patents?**

2 A I d have to check on the timing for that. Again,
3 as I said, my memory is, on their initial declaratory
4 judgment that - I don t believe there was a claim of
5 invalidity. I think it was just that they were upset that
6 PaperTech was getting it free, supposedly. Again, we were
7 filing suit against PaperTech but I guess they didn t know
8 that; and somewhere along the way, they did add the
9 invalidity.

10 So, at the time of the sale from Kobayashi to
11 Equaphor, I believe that claim had been added by Carotex;
12 yes.

13 **Q Did Equaphor obtain any opinions at the time of**
14 **the sale regarding the validity of the patents?**

15 A No.

16 **Q Please turn to Exhibit 10 which is a statement of**
17 **financial affairs, and in particular paragraph ten which is**
18 **Bates stamped 204. There has been some testimony as to the**
19 **5.2-million-dollar liquidating dividend and that Monitoring**
20 **Technology was the largest shareholder; correct? Largest**
21 **preferred shareholder?**

22 A Yes. In October 09, that s correct.

23 **Q How much of that 5.2 million did Monitoring**
24 **Technology receive?**

25 A Monitoring Technology, LLC received 43.5 percent,

1 approximately, of the \$5.2 million.

2 Q And what did Monitoring Technology do with those
3 funds that it received?

4 A I think we put it in the bank.

5 Q Were there any distributions made to any of the
6 members of Monitoring Technology, LLC?

7 A I m sure there were. There were distributions in
8 2009. I m not sure exactly what those amounts were.

9 Q Please turn to Exhibit 8. I believe Exhibit 8 has
10 been entered into evidence. Are you familiar with this
11 document?

12 A Yes.

13 Q In the first line it says, This firm - and it s
14 referring to Stein Sperling - represents Kobayashi. Is
15 that correct?

16 A Yes.

17 Q And Stein Sperling did represent Kobayashi?

18 A Yes.

19 Q And when was this letter sent?

20 A This says April 24, 2008.

21 Q Does that seem accurate?

22 A It seems about right; yeah. It s probably dead-on,
23 I would guess.

24 Q And this letter was sent after the litigation began
25 in New York between Carotex and Kobayashi; correct?

1 A Yes.

2 Q And was Pulp and Paper a client or customer of
3 Carotex at this time?

4 A I think you re off on - the company is actually
5 J.D. Irving and his title is vice president of Pulp and Paper
6 which is a division of J.D. Irving.

7 Q So, J.D. Irving was a customer of Carotex at this
8 time?

9 A As far as I know.

10 Q And did Kobayashi also send a letter to Sunoco?

11 A Sonoco?

12 Q Sonoco.

13 A Yes. I believe.

14 Q Similar letter or just like this one?

15 A Yeah. Well, Stein Sperling sent a letter to
16 Sonoco similar; very similar to this, I would think.

17 Q On Kobayashi s behalf?

18 A Yes.

19 Q Was there another customer of Carotex named Dontar?

20 A Domtar?

21 Q Domtar. And a similar letter was sent by Stein
22 Sperling on behalf of Kobayashi?

23 A I believe that s right; yes.

24 Q Was Georgia Pacific a customer of Carotex at this
25 time?

1 A As far as I know.

2 Q Was a similar letter sent by Stein Sperling on
3 behalf of Kobayashi?

4 A Yes.

5 Q Did Carotex have a customer by the name of SAPPI?

6 A Yes.

7 Q Is that how you pronounce it?

8 A It sure is. South American Pulp and Paper, Inc.,
9 I think.

10 Q Was a similar letter sent to them on behalf of
11 Kobayashi by Stein Sperling?

12 A Yes.

13 Q How about Procter & Gamble? Is that another
14 customer of Carotex?

15 A Yes.

16 Q And a similar letter was sent?

17 A Yes.

18 Q Was Kimberly-Clark a customer of Carotex?

19 A Yes.

20 Q And a similar letter was sent?

21 A Yes.

22 Q And also a customer, New Page?

23 A Yes.

24 Q And a similar letter was sent?

25 A I believe so.

1 **Q Two other companies, Quebecor World and**
2 **AbitibiBowater; is that correct?**

3 A Yeah. AbitibiBowater. A-b-i-t-i-b-I and
4 Quebecor.

5 **Q And similar letters were sent?**

6 A Yes.

7 **Q Were those letters sent at your direction?**

8 A I reviewed and approved this letter; yes.

9 **Q Who else did Stein Sperling represent in the New**
10 **York action with Carotex besides Kobayashi?**

11 A At this time?

12 **Q Or at any time throughout the New York action, who**
13 **have they represented?**

14 A At this time, in April of 08, I believe the only
15 party was Kobayashi. I believe that s right; and so, Stein
16 Sperling was representing Kobayashi in New York. Then, if my
17 memory is right, I think Carotex added - Carotex and ECS I
18 think added me personally and Equaphor in November of
19 December of 2009, I believe, and at that time Stein Sperling
20 represented me personally, as well, and then Stein Sperling
21 also represented Equaphor at that time.

22 **Q Are you aware that Carotex has offered to the**
23 **trustee to settle Carotex s claims against the estate in**
24 **exchange for the estate settling the claims against Carotex?**

25 A You re asking me if I m aware that the trustee has

1 heard an offer for -

2 Q That s correct.

3 A Is it eight million or four million total or four
4 million each?

5 Q All I m just asking right now is if you are aware
6 that an offer was made by Carotex to the trustee.

7 A I - there - I was aware - I believe I was aware
8 of that one. I think there was also an offer made that we
9 just walk away from everything and give Carotex a paid-up
10 license.

11 Q So, you re aware of that?

12 A Is that the one you re speaking of with the fully
13 paid-up license -

14 Q Yeah. Both sides would agree to walk away from the
15 litigation.

16 A Yes. I m aware of that.

17 Q Are you aware if the trustee was agreeable to
18 walking away?

19 A That I don t know. Again, that offer to me, if
20 it s the one I m thinking of, was just made last week, I
21 think.

22 Q Were you not agreeable to walking away from that
23 litigation?

24 A I think it was prior to -

25 MR. MCCARTHY: Your Honor, I have to object to the

1 line of questioning to the extent that it goes other than to
2 what did the trustee know and reasonably consider prior to
3 entering into this deal and I think we re beyond that because
4 we re into last week.

5 THE COURT: I think that s correct. I ll sustain
6 the objection.

7 BY MR. MISKEN:

8 Q In the complaint in the New York action, Equaphor
9 seeks \$3.5 million in compensatory damages; is that correct?

10 A That sounds about right; yes.

11 Q And approximately five million in punitive damages?

12 A It s been a while since I ve look at that, frankly;
13 so, I ll trust what you re saying.

14 Q So, Kobayashi is purchasing from the bankruptcy
15 estate a potential 8.5-million-dollar claim?

16 A I lost your math. 8.5 million?

17 Q Correct. Kobayashi is proposing to purchase the
18 estate s claims against Carotex; correct?

19 A Yes.

20 Q And those claims total approximately 8.5 million?

21 A Again, if you say so. It s been a while since I ve
22 looked at that.

23 Q And you think that Equaphor is likely to succeed in
24 that New York action against Carotex?

25 A I sure believe so.

1 Q Is Kobayashi willing to purchase the patents
2 without the releases?

3 A No, I don t think so.

4 Q In paragraph 4-A of the asset purchase agreement,
5 which is at Exhibit 2, Bates stamped 13, it states that The
6 order approving the sale to Kobayashi must include a specific
7 finding that Kobayashi is a good-faith purchaser of the sale
8 assets. Do you see that? It s Romanette (ii).

9 A Yes.

10 Q If the court did not make a finding that Kobayashi
11 was a good-faith purchaser would Kobayashi still purchase the
12 sale assets?

13 A You know, again, I m - as I said, I m a mechanical
14 engineer. So, sometimes the - and not that I m not familiar
15 with contracts and not reasonably sophisticated here but I m
16 not exactly sure what that means. I m going to have to leave
17 that for counsel.

18 MR. MISKEN: Okay. I have no further questions,
19 Your Honor.

20 THE COURT: Okay. It s about the time I would break
21 for lunch. If you were planning ten minutes of cross
22 examination I would hold off but if it s longer I think we
23 will go ahead and take a lunch break.

24 MR. SHAPIRO: No. It will be longer.

25 THE COURT: Okay. We will go ahead and take a lunch

1 break. We will resume 50 minutes from now which will be at
2 ten minutes of 2:00.

3 (Whereupon, a luncheon recess was taken.)

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THE COURT: Please be seated. I apologize for the
delay in getting back. I believe Mr. Dechman was on the
witness stand.

6

Mr. Shapiro.

7

8

MR. SHAPIRO: Your Honor, I would like to have the
witness shown this document. I have a copy for the court.

9

10

THE COURT: Okay. We will mark it as Bamber s
Exhibit F.

11

(Bamber s Exhibit F

12

was marked for identification.)

13

MR. SHAPIRO: F did Your Honor say?

14

THE COURT: Yes.

15

CROSS EXAMINATION

16

BY MR. SHAPIRO:

17

Q Take a moment to look at Exhibit F and my first

18

question is whether this is a letter that you sent to the

19

shareholders of Equaphor on or about July 28, 2010.

20

A Yes, it is.

21

Q And on the second page, third paragraph, would you

22

read the first sentence of the third paragraph out loud?

23

A If the company is unable to obtain capital it will

24

be deemed insolvent and will cease operations.

25

Q And that is something that you sent in July of

1 2010?

2

3 A Yes.

4 Q And then turning back to the first page of Exhibit
5 F and the fourth paragraph and the fourth line, you say that
6 legals to date are approximately \$900,000 of which 350 had
7 previously been paid by Kobayashi and 550,000 by Equaphor.
8 And when you said 350 had previously been paid by Kobayashi,
9 that s previous to what?

10 A Previous to Equaphor purchasing the patents.

11 Q And the \$550,000 was spent after Equaphor purchased
12 the patents?

13 A Yes.

14 Q And that is what they had spent up to July of 2010?

15 A Yes.

16 Q Did Kobayashi pay any legal fees for the Carotex
17 litigation after the patent sale to Equaphor?

18 A No.

19 Q And what is the total amount that Equaphor has
20 paid for the patent litigation with Carotex?

21 A You know, I m not sure of the precise number but
22 I would guess it s around 800,000; something like that.

23 Q I think you have Exhibit C, the income statement
24 for November 30, 2010 in front of you.

25 MR. SHAPIRO: Your Honor, I confess. I m not sure

1 whether this is admitted before.

2 THE COURT: It was not.

3 MR. SHAPIRO: I didn't think so.

4 BY MR. SHAPIRO:

5 Q Do you have that in front of you?

6 A Yes.

7 Q And is this the income statement for Equaphor for
8 the month ending November 30, 2010 and year to date?

9 A Yes.

10 MR. SHAPIRO: I would like to offer that into
11 evidence, Your Honor.

12 THE COURT: It will be admitted.

13 (Bamber's Exhibit C
14 was received in evidence.)

15 BY MR. SHAPIRO:

16 Q You see the line item, General Legal Expenses,
17 \$803,540?

18 A Yes.

19 Q Were those expenses for the Carotex litigation paid
20 by Equaphor as of that time?

21 A Those are the legal expenses paid by Equaphor at
22 that period of time and as I mentioned earlier I imagine some
23 part of those were for the derivative lawsuit,
24 indemnification and - but the majority would be for the
25 patent work.

1 Q And the \$158,000 paid in November, was that for the
2 patent litigation?

3 A You know, I m not sure. Again, there was some
4 derivative work, the derivative lawsuit work that was more
5 hot around November. So, I m not sure of the breakdown for
6 November itself.

7 Q Do you recall there was a meeting in Wilmington,
8 Delaware in October that you attended and I attended?

9 A Yes.

10 Q And you made a presentation to me?

11 A Yes.

12 Q And there was an extension of the time to respond
13 to the complaint while we continued discussions; isn t that
14 right?

15 A Yes.

16 Q Okay. That extension continued through the
17 December board meeting, the early December board meeting at
18 which you considered or the board considered an offer that I
19 had made; correct?

20 A I believe that s right. Yes.

21 Q There wasn t much going on in the derivative
22 litigation in November; was there? There was certainly no
23 court activity in November; was there, sir?

24 A Not that I m aware of; no.

25 Q So, is it fair to say that most if not all of the

1 **\$158,000 spent on legal expenses in November 2010 were**
2 **related to the Carotex litigation?**

3 A You know, again I m not sure. I don t have that
4 breakdown; but based on what we said, that sounds okay.

5 MR. SHAPIRO: Your Honor, I would like to show the
6 witness several pages, what begins with an email dated May
7 20, 2009.

8 THE COURT: We will mark it Bamber Exhibit G.

9 (Bamber s Exhibit G
10 was marked for identification.)

11 MR. SHAPIRO: If I might clarification one thing,
12 Your Honor. There are some underlinings, obviously added
13 later. So, I m not really offering that as part of the
14 exhibit.

15 THE COURT: I understand.

16 BY MR. SHAPIRO:

17 **Q This May 20, 2009 email, that s something that you**
18 **sent to the board of directors of Equaphor around that time?**

19 A Yes. That s what the heading has here. Yeah.

20 **Q And this was - I think you testified on your**
21 **direct examination there had been discussions with the board**
22 **over a period of time about the sale, possible sale to Cognex**
23 **and how the Management Services Agreement fit into that.**

24 A Yeah. At this point in time - and certainly we
25 were discussing things with Cognex. But this was more of a

1 general review of, trying to clarify some of the text in the
2 MSA for the board.

3 Q And this was discussed at a board meeting?

4 A Yes.

5 Q And there were comments and feedback from the
6 directors and you revised this and sort of updated it to
7 reflect what the consensus of the board was on these issues
8 during the meeting?

9 A Yeah; and I think I m a little -

10 Q Would you just answer my question?

11 A Oh, I m sorry. I m confused a little bit on the
12 third page here as I look at it though. So, I want to be
13 sure I m testifying correctly. So - because there was an
14 email that was sent out prior to the board meeting where we
15 had a model showing different transactions and how the math
16 was done and then some text to try to clarify the terms; and
17 then, as you said, there was an actual board meeting where we
18 reviewed that text line by line and edited it in real-time
19 and then approved each of the changes.

20 So, as I look at this third page, this looks like
21 the - the - the - the work, the work product that we did
22 out of the meeting where we edited and then read back and got
23 approval for each section whereas this first email looks more
24 like the very first email we sent.

25 So, I don t know that these pages go together is my

1 point. They were related to the same meeting and notes but
2 the email - you know, the email mentions an attachment, MTC,
3 progressions current, and that s not the attachment. This
4 third page is not that attachment. That attachment was an
5 Excel spreadsheet.

6 Q I didn t mean to suggest it was by marking the
7 exhibit, Mr. Dechman.

8 But the text in your May 20 email, which is the
9 first page carried over to the top of the second page of
10 Exhibit G, was revised in light of the discussion at the
11 board meeting; correct?

12 A Well, the email wasn t revised. This was, you
13 know, text that was sent prior to the board meeting. Then
14 yes, during the board meeting we went through this text line
15 by line and edited it.

16 Q And the edits are reflected on the third page; are
17 they not?

18 A I believe that s right. But the Excel model that
19 was attached here isn t - you know, it s not a complete
20 document. That s all.

21 Q I d like to direct your attention to paragraph
22 number five that begins Book value of assets and
23 liabilities, et cetera.

24 A Yes.

25 Q In the last sentence of that paragraph you wrote,

1 **One or more companies may pool to conduct this transaction**
2 **and satisfy the sale of substantially all assets. Do you**
3 **see that, sir?**

4 A Yes, I do.

5 **Q What did you mean by satisfy the sale of**
6 **substantially all assets?**

7 A The text that was in the MSA stating about - you
8 know, there s text in there about what substantially all
9 assets means.

10 **Q The sale was defined as a sale of all or**
11 **substantially all of the assets that triggered the sale**
12 **incentive fee; correct?**

13 A I believe that s right. Yeah.

14 **Q And the board meeting took place on May 27, 2009;**
15 **did it not?**

16 A That I don t know but I m sure it was around that
17 time period.

18 MR. SHAPIRO: I would like to offer the May 27, 2009
19 board minutes.

20 THE COURT: Okay. We ll mark it as Exhibit H,
21 Bamber s Exhibit H.

22 (Bamber s Exhibit H
23 was marked for identification.)

24 BY MR. SHAPIRO:

25 **Q Take a moment to read it, Mr. Dechman. But is**

1 Exhibit H the minutes of the board meeting on May 27, 2009?

2 A Yes.

3 Q And did you prepare the minutes? I see it has your
4 name at the bottom.

5 A Yes, I did.

6 Q Okay. And that was done on June 4, 2009, as
7 indicated by the date at the top?

8 A I believe that s right.

9 Q Okay. And in paragraph two, Soze Commission. Is
10 it Soze or So-ze? I m sorry.

11 A So-ze.

12 Q So-ze. And Soze was a character in the movie,
13 The Usual Suspects; is that right?

14 A Yes.

15 Q And Kobayashi was also a character in the movie?

16 A Yes.

17 Q They were the bad guys; weren t they?

18 A (Laughter.)

19 BY MR. SHAPIRO:

20 Q You wrote under paragraph two, In an effort to
21 better clarify the Management Services Agreement between MTC
22 and Soze, the board reviewed a letter and spreadsheet model
23 prepared by Jim Dechman. That was the letter that s an in
24 email form here. It s the first page of Exhibit G with
25 the - is that right?

1 A Yes.

2 Q And then you wrote: During the meeting Mr. Dechman
3 updated the letter to better capture the agreement. And the
4 third page is the updated letter to better capture the
5 agreement, correct, the third page of Exhibit G?

6 A Yes.

7 Q And then in paragraph five, the last sentence of
8 the May 20 email, One or more companies may pool to conduct
9 this transaction and satisfy the sale of substantially all
10 assets. If you turn to the third page of Exhibit G and you
11 look at paragraph five that begins Book value of assets and
12 liabilities, that s the paragraph again in the May 20 email;
13 correct?

14 A Yes.

15 Q And then if you look at the box over on the right
16 where it says, Deleted, and the second sentence in the
17 deleted box is, One or more companies may pool to conduct
18 this transaction and satisfy the sale of substantially all
19 assets. You deleted that from the outline; correct?

20 A Yes.

21 (Pause.)

22 BY MR. SHAPIRO:

23 Q I digress for a moment. Do you have in front of
24 you Exhibit A which is the minutes of the December 7, 2010
25 board meeting? I have an extra copy here if you need it.

1 A I have them.

2 Q And are these the minutes of that meeting?

3 A I m sorry.

4 Q The document in front of you marked A, are those
5 the minutes of the December 7, 2010 board meeting?

6 A Yes.

7 MR. SHAPIRO: I would like to offer that into
8 evidence at this time, Your Honor.

9 THE COURT: It will be admitted.

10 (Bamber Exhibit A
11 was received in evidence.)

12 (Pause.)

13 MR. SHAPIRO: I will offer, Your Honor, the
14 September 25, 2007 email.

15 THE COURT: We will mark it as Bamber I.

16 (Bamber Exhibit I
17 was marked for identification.)

18 BY MR. SHAPIRO:

19 Q Looking at the email, dated September 25, 2007 in
20 Exhibit I, is that an email that you sent to the three
21 directors and copied Mr. Fiore on September 25, 2007?

22 A Yes.

23 Q And in paragraph 1-B, you wrote: As a condition of
24 the royalty agreements, KV must not be owned or associated
25 with a competitor of the licensees and therefore MTC cannot

1 be involved. There was no provision in the royalty agree-
2 ment that prohibited Equaphor from owning the patents; was
3 there?

4 A No. There was a provision that talked about if a
5 competitor acquired the license agreements that the licensee
6 had the right to terminate.

7 Q But nothing that prohibited Equaphor from
8 purchasing the patents?

9 A Again, as I said, Equaphor tried to buy these
10 patents three or four times over the years.

11 Q But Equaphor didn't try to buy them in September
12 2007; correct?

13 A No.

14 Q In the beginning of the email you said, The
15 International Paper patent negotiations are nearly complete.
16 Who conducted those negotiations with International Paper?
17 What person or persons?

18 A It was Jacklin and an attorney, Jay Spitson.

19 Q So, Jacklin was essentially a straw that you used
20 to purchase the patents?

21 A As I said before, yeah, we engaged Jacklin to
22 negotiate a deal and then sell, immediately sell the
23 portfolio to Kobayashi.

24 Q And it says in paragraph 1-C, little one, two, I
25 guess, that Kobayashi will retain the law firm, Stein

1 Sperling (Jeff Schwaber) to enforce the agreements, pursue
2 infringements, et cetera. Correct?

3 A Yes.

4 Q Stein Sperling was Equaphor s law firm up until
5 September 2009; was it not?

6 A Stein Sperling did work for Equaphor, as did
7 Whiteford Taylor.

8 Q And Mr. Schwaber is here in the courtroom, at
9 counsel table?

10 A Yes, he is.

11 Q You said that you believed that \$225,000 is the
12 total amount that was paid to - paid by Kobayashi to
13 purchase the patents; is that right?

14 A Yes.

15 Q My question is, did that include the money that
16 was paid to Jacklin, that Jacklin paid to International
17 Paper?

18 A Yes. To be carefully slow on it, Kobayashi paid
19 Jacklin. I believe it was 80,000. Jacklin paid
20 International Paper 75,000 of that 80,000; and then Kobayashi
21 later paid 150,000 directly to International Paper.

22 Q So, International Paper at that point knew that
23 Kobayashi owned the patents?

24 A They knew immediately after the transaction because
25 the patents were transferred from Jacklin to Kobayashi.

1 Q And you said that International Paper wanted to
2 have someone own the patents who would have the ability to
3 pursue royalty claims because International Paper was to get
4 50 percent of anything collected after expenses; correct?

5 A I believe that s what - they were interested based
6 on the way they negotiated the agreement.

7 Q And Jacklin was basically a shell company formed
8 for the purpose of acting as a straw for Kobayashi; wasn t
9 it?

10 A No.

11 Q No? What was Jacklin?

12 A Jacklin I believe is an accounting company. It s
13 been around for many years.

14 Q Molly Hale is and has been for some time an
15 employee of Monitoring Technology?

16 A Yes. Molly Hale was an employee of Equaphor and
17 now she s an employee of Monitoring Technology, LLC.

18 Q And there was a board meeting scheduled in
19 September 2009 to consider approval of the sale to Cognex,
20 the purchase of the remaining business assets by Monitoring
21 Technology and the sale of the patents from Kobayashi to
22 Equaphor; correct?

23 A Yes.

24 Q And the board at that time? There were four
25 directors; correct? There s Mr. Evans, Mr. Kaufman, Mr.

1 **Spiva and Mr. Doherty?**

2 A Yes. Prior to adding Molly Hale to the board,
3 that s correct.

4 Q And was it your understanding prior to the meeting
5 that Mr. Spiva and Mr. Doherty would vote in favor of this
6 transaction? Is it your belief that they would?

7 A Yes. I thought they would.

8 Q And you expected that Mr. Kaufman would oppose the
9 transaction; did you not?

10 A You know, I m not sure whether he would or not. But
11 I wasn t sure he would support it; no.

12 Q And had you had any discussions with Mr. Evans
13 about his position?

14 A I don t remember. I know we - we scheduled a board
15 meeting and it was - you know, sometimes we had a board
16 meeting remotely where all these folks would dial in because
17 some were in Boston, and Philly, and Baltimore; and for this
18 one, we had called an in-person meeting. And I know Mr.
19 Evans and Mr. Kaufman had both said they were coming but then
20 one of them said they couldn t and then the other one said
21 that he couldn t. So, they attended by phone.

22 Q Did you have any discussions with Mr. Evans prior
23 to the meeting as to how he would vote?

24 A Not that I recall.

25 Q So, you didn t know how he would vote?

1 A I wasn t sure; no.

2 Q And Miss Hale was elected as a director immediately
3 prior to the meeting; correct?

4 A Yes.

5 Q And it was done by a consent, majority of the
6 Series - one of the preferred series other than F. Let me
7 back up just a minute. There were a number of different
8 series of preferred stock in Equaphor; were they not?

9 A Yes.

10 Q And one of the series of was a D that had the
11 right to elect a director?

12 A Actually it was Series E had the right to elect
13 another director.

14 Q And between Monitoring Technology and Mr. Spiva and
15 Mr. Doherty, the three controlled the majority of the
16 Series E shares; correct?

17 A Yes.

18 Q And so, the three of you, Monitoring Technology,
19 Mr. Spiva on behalf of the venture capital fund that owned
20 the shares and Mr. Doherty on behalf of the venture capital
21 fund he was associated with, the three voted the shares to
22 elect Miss Hale director?

23 A Yes.

24 Q And that was done minutes before the meeting
25 started; was it not?

1 A It was done immediately prior to the meeting; yes.

2 Q And that gave you three directors to vote in favor
3 of the transaction?

4 A Assuming that Molly Hale would vote in favor, yes.

5 Q It was a safe assumption, was it not? She worked
6 for you?

7 A Well, you d have to know Molly. But you know, you
8 never know. I m sure she would vote what she thought was
9 right.

10 Q Do you recall the date of the board meeting?

11 A I m sorry, Mr. Shapiro.

12 Q Do you recall the meeting was on September 23,
13 2009?

14 A You know, I m not sure of the exact date.

15 MR. SHAPIRO: I would like to offer a memo.

16 THE COURT: We ll mark it as Bamber Exhibit J.

17 (Bamber Exhibit J

18 was marked for identification.)

19 BY MR. SHAPIRO:

20 Q Is Exhibit J a memorandum that you wrote on
21 September 21, 2009?

22 A Yes.

23 Q And this was circulated to the directors at that
24 time?

25 A Yes.

1 **Q And you recall it was just two days later when the**
2 **directors held a meeting to approve the transactions?**

3 A I mean, I know we had been talking about these
4 transactions for nine months and I can t remember the date of
5 the actual board meeting; but two days sounds probably about
6 right.

7 **Q Well, a sale to Cognex had been discussed for many**
8 **months; had it not?**

9 A Yes.

10 **Q Was a sale of the patents to Equaphor discussed in**
11 **advance of September 21?**

12 A I may have discussed it with J.B. Doherty or Ed
13 Spiva before.

14 **Q You didn t discuss it with Sumner Kaufman before**
15 **September 21; did you, sir?**

16 A Not that I remember.

17 **Q And you hadn t discussed with Mr. Kaufman before**
18 **September 21 the proposal that Soze, later named MTC, would**
19 **buy all the assets not bought by Cognex; did you?**

20 A I m not sure. I mean, we certainly talked about
21 having multiple parties buy the assets in those different
22 board meetings.

23 **Q Originally Cognex was to buy the entire company;**
24 **was it not?**

25 A When we first met with Cognex, yes. About a year

1 prior to that, we were hoping that they would buy the whole
2 thing.

3 **Q And when was it that they made a decision they only**
4 **wanted to buy the Smart Advisor video business?**

5 A As I said, we met with them in the fall of 2008,
6 good meetings, and their CEO and founder attended the
7 meeting, and it seemed like things were going along pretty
8 good; and then they went silent, and -

9 **Q It s a simple question. When did they tell you**
10 **they were only interested - when did Cognex tell you it was**
11 **only interested in buying the Smart Advisor video business**
12 **and not the other businesses?**

13 A And I appreciate it. I m not trying to be verbose
14 here but I m not sure exactly when the date was. So, I ll
15 leave it at that, I guess.

16 **Q Can you tell us approximately when it was?**

17 A As I said: So, we had some conversations and then
18 they went silent. When we started having conversations
19 again, they seemed more interested in just the Smart Advisor
20 video business and so that started that focus which would
21 have been I guess around May, May of 2009.

22 **Q And the board on September 23, 2009 approved the**
23 **three transactions; correct?**

24 A Well, as I said before, you ve given that date
25 before and I ll trust you that that s it. That sounds about

1 right.

2 Q And it was approved by the vote of Mr. Spiva, Mr.
3 Doherty and Molly Hale?

4 A Yes, with Evans abstaining and Kaufman dissenting.

5 Q You re not claiming that the patents when they were
6 sold to Equaphor were worth \$3,450,000; are you?

7 A No. I mean, there was no valuation done on it.
8 You know, so it was more that - it was an alternative deal
9 structure than the one that was in the MSA.

10 Q So, the purchase price of \$3,450,000 was calculated
11 based on what you claimed the sale incentive fee would be to
12 Soze; correct?

13 A No. It was based on three things, as I said
14 before, the sales incentive fee to Monitoring Technology, LLC
15 that was around one and half million; the third year of the
16 Management Services Agreement which was a million, and the
17 patent liability, patent royalty liability which was 900,000.

18 Q At the time Kobayashi bought the patents from
19 International Paper there was an accrued royalty liability of
20 640-some-odd-thousand dollars to International Paper;
21 correct?

22 A Yes.

23 Q And didn t you advise the board that because some
24 other licensees were not paying International Paper that
25 Equaphor didn t need to pay it under the most favored nation

1 **provision of the royalty agreement?**

2 A We tried that argument with International Paper
3 back - back when we were trying to buy the patents from IP,
4 one of the first times. So, Equaphor tried that argument
5 just as a letter and hoping that International Paper would
6 either start to enforce the patents equally to level the
7 playing field or that they would agree, you know, and then
8 the playing field would be level; and then, IP didn t, didn t
9 accept that position.

10 Q Well, regardless of what IP s position was, wasn t
11 it your position as president of Equaphor that the most
12 favored nation provision gave Equaphor the right not to pay
13 the 640,000-dollar royalty?

14 A Well, again, as I said, we had counsel -

15 Q Can you answer that yes or no?

16 A I don t think I can because, again, we had counsel
17 and counsel suggested that we send the letter out but they
18 also suggested that it was a weak position and, you know,
19 we d just see what would happen.

20 Q But for whatever reason, Equaphor didn t pay the
21 money and International Paper never pressed for payment; did
22 it?

23 A Not at that time; no. Not especially.

24 Q And two years went by without International Paper
25 having pressed for that money?

1 A That s correct; and we kept accruing the liability
2 on the books.

3 Q That was your decision to accrue the liability?

4 A No. It was the board s decision.

5 Q You approached the board and said that you wanted
6 to buy the patents back in 2007 and you got the board to give
7 a conflict of interest waiver; did you not?

8 A Well, we - I don t know if you d call it conflict
9 of interest but we had the board agree to a waiver to allow
10 us to do the purchase.

11 Q Well, a waiver of any claims against you or
12 Kobayashi on account of Kobayashi purchasing the patents?

13 A I believe that s right; yeah.

14 Q And then Stein Sperling went to the board and said,
15 we d also like a waiver of any claims against Stein Sperling
16 on account of our having been counsel to the company and now
17 representing Kobayashi in this patent business; correct?

18 A Yes.

19 Q And Mr. Spiva and Mr. Doherty and Mr. Evans agreed
20 to those?

21 A Yes.

22 Q And was there any discussion at that time about
23 whether the company would owe you or Kobayashi the \$640,000
24 on the accrued royalty?

25 A Yeah. I think - I mean, we d need to pull the

1 patent waiver agreement out. I haven't looked at it for a
2 little bit but I think there might have been a sentence even
3 in there about that.

4 **Q You remember that or are you speculating?**

5 A I guess I am speculating. I'd have to see the
6 document, to read the sentence; but my memory is that it
7 was - that Kobayashi was free and clear to pursue the patent
8 enforcement, and the objective was to level the playing field
9 and market.

10 **Q You recall Mr. Evans asking about what's going to**
11 **happen with this \$640,000 and you said don't worry about it?**

12 A No, I don't recall that.

13 **Q Do you have the waiver agreement with you here?**

14 A I don't have it here, I don't think. I think it's
15 in -

16 **Q It's not in front of you, as far as I know. Did**
17 **you bring it with you to court?**

18 A I don't think I did.

19 **Q So, getting back to the sale of the patent to**
20 **Equaphor, \$900,000 of what Equaphor paid Kobayashi**
21 **represented this accrued royalty obligation?**

22 A Yes.

23 **Q And Equaphor could have bought the patent for**
24 **\$225,000 and been rid of that obligation; couldn't it?**

25 A I don't think so.

1 **Q You don t think Jacklin could have bought it as a**
2 **straw for Equaphor just as it bought it as a straw for you?**

3 A Well, I think if it had done that - I mean, again,
4 a lot of things transpired before those two deals. And
5 again, just in a hypothetical, you know, maybe Equaphor could
6 have bought it using Jacklin as a straw for the 75 up front
7 and the 50-percent enforcement but then Equaphor would be
8 faced with - you know, I don t think it could just waive its
9 royalty without paying IP some of that based on the intent of
10 the agreement. And of course, after we purchased it and
11 before we purchased the remaining piece for the 150, we had
12 invested heavily on legal fees and enforcement. So, Equaphor
13 would have had to invest in it, as well. It s hard to say.

14 **Q Isn t possible that one of the ways the**
15 **transactions could have been conducted in September of 2009**
16 **was that Equaphor just pay Kobayashi the \$3,450,000 and you**
17 **keep the patent? That would have worked out the way you**
18 **figured the math based on the sale incentive fee and the**
19 **royalty obligation. That would have -**

20 A Well, part of the -

21 **Q Could you just answer the question? It could have**
22 **just paid the three-million-four-fifty. That would have been**
23 **full payment to Kobayashi or whatever Kobayashi was owed and**
24 **Kobayashi could have kept the patents. Isn t that right?**

25 A I guess the deal could have been structured any

1 way but there were advantages to having Equaphor own the
2 patents.

3 Q Well, one of the advantages was that if Equaphor
4 owned the patents it had to pay the expenses for the Carotex
5 litigation; correct?

6 A Well, yeah. I mean, if they bought the -

7 Q Okay. You've answered the question.

8 Now, at the time the patent was sold, you had an
9 agreement in principle with PaperTech for PaperTech to pay
10 \$690,000; did you not?

11 A No.

12 Q No? How soon after the patent sale did you get the
13 \$690,000 from PaperTech?

14 A Very quickly.

15 Q Okay.

16 A But it was in court as a negotiated settlement with
17 Judge Preska in New York and it was by no means a clear
18 outcome for that.

19 Q You had this settlement agreed to with PaperTech
20 subject to court approval?

21 A No. We had reached a settlement for I think
22 around 800,000 and then PaperTech backed out and they were
23 getting real excited and upset and the judge ordered us back
24 up to court to try to sit down and have another settlement
25 discussion and that happened on I think October 1st or 2nd.

1 Q **Didn t you testify in response to questions by Mr.**
2 **McCarthy that you either had or thought you had a deal with**
3 **PaperTech and therefore you were optimistic that Carotex**
4 **would follow suit and you could settle with Carotex, as well?**

5 A Sure. Yeah. I mean, again, we had a -

6 Q **And that was your thinking at the time you sold the**
7 **patent to Equaphor; wasn t it?**

8 A As I said - I think I said it correctly before. We
9 felt like we had reached a deal with PaperTech and they
10 backed down and then we were going up to see the judge in New
11 York to hammer out a deal. Then she had us leave the room and
12 give her numbers that we would take. I mean, it was a full-
13 fledged negotiation. I mean, you know, that -

14 Q **At the time you sold the patent to Equaphor, you**
15 **thought you had a deal with PaperTech?**

16 A We thought we could get to a deal with PaperTech.
17 Yeah.

18 Q **And you thought that if you got to a deal with**
19 **PaperTech there was a good chance that Carotex would follow**
20 **suit and you could settle with Carotex?**

21 A We had hoped that was the case; and Equaphor, you
22 know, by owning the patents had this, you know, lost profit
23 claim that it could bring and, you know, it had some
24 different material claims that it could bring which made it a
25 better holder for the patents.

1 **Q** But you didn't put a value on those claims or those
2 considerations in deciding on the 3,450,000-dollar purchase
3 price? That was driven by what was owed on the management
4 agreement and the sale incentive fee and the royalties;
5 correct?

6 A That's correct, and -

7 **Q** So, the other claims you gave to Equaphor for free?

8 A Right; and then the other -

9 **Q** Okay. You've answered my question.

10 MR. REYNOLD: Your Honor, Mr. Shapiro keeps on
11 interrupting Mr. Dechman.

12 THE COURT: Do let the witness answer the question.

13 THE WITNESS: Thank you.

14 MR. SHAPIRO: I think he's going beyond the
15 question, Your Honor, but okay.

16 BY MR. SHAPIRO:

17 **Q** Go ahead.

18 A You were asking kind of what all went into the
19 deal and the other piece of the deal was - and I mentioned
20 it earlier but was the non-compete piece that all worked
21 into that total deal.

22 **Q** So, part of the patent sale to Equaphor included a
23 provision that any royalties collected on account of the
24 patents within a year of the sale would be paid over to
25 Kobayashi; correct?

1 A Yes.

2 Q And so, the \$690,000 that was paid by PaperTech
3 after the sale to Equaphor, Equaphor received it and paid it
4 right over to Kobayashi?

5 A Yes.

6 Q And in fact, you had caused Equaphor - you caused
7 that to be treated as an additional purchase price paid for
8 the patent; didn't you?

9 A That's what the tax accountants told me to do.

10 Q And then Equaphor had to treat that \$690,000 as
11 ordinary income and you got to treat it as a capital gain
12 when you received it, didn't you?

13 A It's what the tax folks said to do.

14 Q Your tax lawyer?

15 A No, I'm not a tax lawyer.

16 Q I said, your tax lawyer, advising Kobayashi -

17 A Actually both. They met together and discussed it.

18 Q So, if your hope or expectation that you could
19 settle with PaperTech and then settle with Carotex proved to
20 be true then all the money that came in from those settle-
21 ments would go to Kobayashi, notwithstanding that the patents
22 had been sold to Equaphor; correct?

23 A Yes.

24 Q And if your hope or expectation turned out not to
25 be true and this expensive litigation with Carotex continued

1 on then Equaphor would have the burden of the expense of that
2 litigation, wouldn't it?

3 A Yes.

4 Q Sort of a win-win for Kobayashi; wasn't it, sir?

5 A I mean, if you state it that way. I mean, the
6 500,000 in Equaphor was a note provided by Kobayashi. So,
7 the money was coming from Kobayashi and we owned 83.5 percent
8 of Equaphor. So, it wasn't that much of a win-win, I don't
9 think.

10 Q Now, Mr. McCarthy asked you about - I'm sorry.
11 Mr. Miskin asked you about a series of letters that Mr.
12 Schwaber sent on your behalf to customers of Carotex. Do
13 you recall that, sir?

14 A Yes.

15 Q And I think you testified that you authorized those
16 letters.

17 A Yes.

18 Q And you did that on behalf of Kobayashi; did you
19 not?

20 A Yes.

21 Q And the purpose of those letters was to try to
22 enforce a royalty or licensing agreement so that Kobayashi
23 could collect royalties?

24 A Yes; and I should - you know, those letters were
25 sent on advice of counsel. So, it was part of a strategy

1 meeting with counsel and they suggested sending the letters
2 and I authorized it.

3 Q And that was counsel for Kobayashi, Stein Sperling?

4 A There were other counsel involved, too, but it was
5 counsel for Kobayashi.

6 Q Various law firms representing Kobayashi?

7 A I think Finnegan. Finnegan was involved at that
8 point and -

9 Q Right. There were no lawyers for Equaphor involved
10 in sending letters on behalf of Kobayashi, were there?

11 A No.

12 Q And you didn't do this on behalf of Equaphor; did
13 you, sir?

14 A No.

15 Q And do you understand, sir, that the damage claim
16 against Equaphor that has been asserted by Carotex and ECS is
17 based primarily on the letters that you sent on behalf of
18 Kobayashi?

19 A Yes.

20 MR. SHAPIRO: Thank you. I have no other questions.

21 Can I have just one minute, Your Honor?

22 (Counsel confer.)

23 MR. SHAPIRO: Your Honor, I think the exhibits that
24 were referred to earlier that weren't admitted have now been
25 admitted. I think there were just two that have now been

1 admitted, the balance sheet and the board minutes.

2 THE COURT: Those two have been admitted.

3 MR. SHAPIRO: I have no other questions.

4 THE COURT: Okay. Any redirect, Mr. McCarthy?

5 REDIRECT EXAMINATION

6 BY MR. MCCARTHY:

7 Q Mr. Dechman, the judge asked me when I as on the
8 stand whether we were attempting to affect the Carotex
9 license, if any, by virtue of that language within the
10 adversary - the APA, and I think I answered not that I know
11 of. Could you clarify that from your standpoint, please?

12 A I ll do the best I can. I think as you said, there
13 are three paid-up licenses. Cognex has a paid-up license;
14 Honeywell has a paid-up license, and PaperTech has a paid-up
15 license. Clearly all of those three are paid up and will -
16 you know, they still - they ll retain their same license
17 agreements.

18 And Your Honor asked a question about Carotex.
19 Carotex terminated their license agreement during the lawsuit
20 and I assume whatever the judge in New York decides around
21 their license is what it should be. So, she - I don t know
22 if that s clear enough or not.

23 We have no intention of using this process to
24 short-circuit any licensing with Carotex; but to the extent
25 that the judge in New York says the license is intact or is

1 not, we would honor whatever she says.

2 Q All right. On the issue of the MSA and the
3 reference in it to the formula that applies if substantially
4 all assets are sold, I believe Mr. Shapiro questioned you
5 about whether or not that applied in this situation since
6 Cognex of course did not buy all of the assets. What was
7 your understanding as to the applicability of that part of
8 the MSA and as to the board s consideration of that, as well?

9 A Sure. Yeah. From my perspective, there were three
10
11 board members when the MSA was done and they obviously had
12 counsel; and those three board members during the summer of
13 2009 and again during the deal time in September of 2009 all
14 either voted for the deal or later said that they abstained
15 because there just wasn t time to review it and they re fine
16 with it now.

17 So, the authors of the MSA agreed to it all later
18 and, you know, during the minutes - Mr. Shapiro had me
19 review the minutes and showed the section that was deleted
20 about pooling interests, and the discussion at the board
21 meeting was that that was too limiting, that two companies
22 didn t need to pool their interest; it could just be two
23 acquirers buying substantially all the assets. And if you
24 look at the rest of the minutes, it talks about acquire and
25 acquirers. And I d say that is what was discussed.

1 I d further say that when we had the board meeting
2 to do the transactions, the same people either voted for it
3 or abstained, and then the one that abstained came back later
4 and said the deals were proper and -

5 Q And did you and I talk about this question of
6 whether or not the sale of substantially all assets in the
7 MSA was triggered by the structure of the deal in 09?

8 A Yes.

9 MR. McCARTHY: I don t have any more questions, Your
10 Honor.

11 THE COURT: Thank you for testifying. You may stand
12 down.

13 MR. McCARTHY: Your Honor, I would like to call J.B.
14 Doherty.

15 THE COURT: Mr. Doherty, if you will come forward,
16 stand in front of the clerk and be sworn.
17 Whereupon,

18 JOHN BRUCE DOHERTY
19 was called as a witness and, having been first duly sworn,
20 was examined and testified as follows:

21 DIRECT EXAMINATION

22 BY MR. McCARTHY:

23 Q Good afternoon, Mr. Doherty. Would you please
24 state your name and address for the court?

25 A It s John Bruce Doherty. My address is 212

1 Cheswold Hill Road, Haverford, Pennsylvania.

2 **Q Okay. Could you please briefly tell the court**
3 **about your educational background?**

4 A I graduated from the United States Naval Academy
5 with a Bachelor of Science in Engineering degree; and then
6 after Vietnam, I went to Stanford and got an MBA in Finance.

7 **Q What has your work background been since then?**

8 A I was recruited out of Stanford to join a Wall
9 Street investment banking firm, Blyth, Eastman Dillon, where
10 I worked in corporate finance. I was then recruited away
11 from there by a private equity firm that was then advising
12 the Ford Foundation and its direct, private, negotiated
13 investments and remained at that partnership until 1992, 93;
14 and through that history, I was acting as a principal in
15 direct, private, negotiated, also known as venture capital
16 or private equity deals beginning in 1976, and I did so
17 reasonably successfully. We were the seed capital in the
18 ESPN. We were the original equity investor in Airgas which
19 is a very large, publicly-owned company, the largest
20 independent, industrial gas distributor in the country.

21 By the time of this transaction, I was the managing
22 general partner of a private equity fund that was the
23 investor.

24 **Q What was your position with the debtor in 2007?**

25 A In 2007, I was a director.

1 Q And did you have some stock ownership at that time,
2 as well?

3 A Not personally. The fund that I managed was a
4 substantial investor and held E and F, preferred.

5 Q Okay. And that fund combined with whatever entity
6 that Mr. Spiva controlled added up to what percentage of
7 ownership of stock at that time?

8 A As among Vimac, which was the fund John Evans
9 managed, and the fund managed by Ed Spiva, and ourselves,
10 that s the 76 percent that we ve been referring to.

11 Q Is that 76 percent of Series F?

12 A That s correct.

13 Q Which is the only series that gets paid -

14 A We ve got an economic stake by then.

15 Q All right. You ve heard Mr. Dechman describe the
16 07 transactions. I won t ask you to go back over them
17 unless there was something that you heard that, you know, you
18 want to correct from your standpoint.

19 A What I ve heard is completely consistent with my
20 recollection. These things were considered carefully. We
21 had counsel advising us and they were interpreted in good
22 faith throughout the process.

23 Q Who was the counsel in 07?

24 A George Lawler, maybe. The firm, Whitford [sic]
25 Taylor? He has been correctly described previously.

1 Q What was your understanding of what was going to
2 happen to those business - what was going to happen if Mr.
3 Dechman and Mr. Fiore were unable to sell the business within
4 three years of the Management Services Agreement?

5 A We had with, you know, clear-eyed intent
6 established an arrangement where they were obligated to
7 continue to run the business for no further consideration.

8 Q And what was the reason for that? And, you know,
9 if you could add anything else to the reasons for the
10 transaction in 07 other than what Mr. Dechman has already
11 told the court. Could you tell the court?

12 A I think as previously stated, the intent was to
13 align the interests of management and the shareholders in
14 general and to do so in a way that increased the likelihood
15 that the business would be sold at some point in the
16 foreseeable future and not simply revert to, you know, a
17 convenient vehicle for its management.

18 The investors had been invested in this company for
19 a very, very long time and they had invested in the company
20 with the expectation of a return on investment.

21 Q Okay. And as to the 09 transactions, you ve also
22 heard Mr. Dechman describe those. Is there anything that you
23 want to add to his describe or alter as to his description of
24 those transactions in 09?

25 A No; only that I was at the time worried about the

1 economy in which we found ourselves and the environment in
2 which this company would have to be operating going forward
3 and the difficulty of doing any kind of a deal in that
4 environment, as well as the reputation that Cognex had for
5 being a difficult party to close transactions with.

6 **Q Now, you said that you and Mr. Spiva controlled**
7 **the funds that owned collectively about 76 percent of the**
8 **Series F stock back in 07. What did you eventually -**

9 THE COURT: I think he said his fund, Mr. Spiva s
10 funds, and Mr. Evans fund owned 76 percent; but you said
11 just the two.

12 MR. McCARTHY: I did.

13 BY MR. McCARTHY:

14 **Q Is the judge right or am I?**

15 A The judge is right. Sorry. There were three
16 significant funds and each one of those funds actually had a
17 director on the board. So, John Evans represented about a
18 third of the 76 percent; I represented or - and so on.

19 **Q Okay. And all three of you voted for the 07**
20 **transactions?**

21 A That s correct.

22 **Q And what happened to your stock and to Mr. Spiva s**
23 **stock and to Mr. Evans stock after 07?**

24 A Well, I guess the first thing that happened was
25 contemporaneously with all of that we sold a portion of it to

1 I guess MTC, LLC.

2 Q Monitoring Technology, LLC?

3 A Yes.

4 Q Okay. So, you sold some of it to Monitoring
5 Technology, LLC. That was part of the three-way transaction
6 Mr. Dechman described?

7 A Yes.

8 Q Okay. And then, did there come a time when you
9 sold the rest of it?

10 A As described earlier, at the time of the Cognex
11 sale or shortly thereafter there was a big liquidating
12 dividend and then thereafter we sold the balance of our
13 shares.

14 Q And when you say we, you re talking about all
15 three of you?

16 A Ultimately, yes; not in locked step but in a very
17 short period of time.

18 Q And you guys again were majority shareholders
19 effectively in 07. How did those of you who sold your stock
20 fare relative to those who didn t sell their stock?

21 A Well, perversely, the people who took the
22 obstructive view actually did better. I will say that we
23 felt we were being good citizens on behalf of the corporation
24 because we were willing to sell basically half of our
25 position to achieve this alignment with management and the

1 minority hold-out group actually enriched itself by being
2 obstructive at that point.

3 Q Okay. Now,, did you and I have a conversation on
4 March 15

th?

5 A Yes.

6 Q Do you recall the gist of that conversation?

7 A You were asking me about these sorts of things and
8 I think trying to establish whether we understood what we
9 were doing and understood what we agreed to and -

10 Q Do you recall whether or not you and I talked about
11 the issue of whether Equaphor itself could have purchased the
12 patents, at least legally speaking, directly from IP?

13 A We talked about that; and at that time, I shared
14 with you my perspective which was that from an institutional
15 investor standpoint we regarded that, that initiative as
16 being a distraction and, you know, possibly dilutive in terms
17 of the corporate resources. So, it wasn't just a matter of
18 waiving a conflict. Certainly speaking for myself, my fund,
19 my position as a director, I was quite comfortable encourag-
20 ing them to go off and pursue that.

21 Q Do you recall whether we talked about whether
22 legally Equaphor could have owned the patents had you all
23 decided that that was what you wanted?

24 A I think we talked about the fact that I thought
25 they could but that it might prejudice their ability to

1 enforce them vis-a-vis others.

2 Q Okay. Do you recall whether we discussed whether
3 there was anything else of a material nature that you felt
4 you hadn t been apprised of?

5 A We talked about that and I am sure that I assured
6 you that I didn t think that there was anything that we
7 hadn t been apprised of.

8 MR. McCARTHY: I don t have any more questions, Your
9 Honor.

10 THE COURT: Cross examination.

11 CROSS EXAMINATION

12 BY MR. MISKEN:

13 Q Good afternoon, Mr. Doherty. Are you paying any
14 consideration for the release under the asset purchase agree-
15 ment?

16 A I m sorry.

17 Q Under the asset purchase agreement, you obtained
18 a release from any cause of action. Are you paying any
19 consideration in exchange for that release?

20 A No.

21 MR. MISKEN: I have no further questions, Your
22 Honor.

23 CROSS EXAMINATION

24 BY MR. SHAPIRO:

25 Q Did I understand you, Mr. Doherty, that back in

1 07, you were of the view that Equaphor could legally acquire
2 the patents but it just wouldn't be a good business thing for
3 Equaphor to do that? Is that the substance of your testimony
4 about what the -

5 A Yes.

6 Q Okay. Would you look at Exhibit I in front of you?
7 It's an email from Mr. Dechman. It's dated September 26th at
8 the top and then halfway down there's a September 25 email.
9 Do you have that in front of you?

10 A I do.

11 Q In the September 25 email, if you'd would look down
12 to paragraph one, little b. As a condition of the royalty
13 agreements KV must NOT - capital letters, N-O-T - be
14 owned or associated with a competitor of the licensees and
15 therefore MTC cannot be involved. Were you of the view that
16 that was not true?

17 A I'm not sure I remember that specific phrase.

18 Q You didn't read the royalty agreements back then;
19 did you?

20 A I don't know.

21 Q Didn't you rely on Mr. Dechman for his advice about
22 the situation when you approved Kobayashi buying the patents?

23 A I said I didn't know.

24 Q You don't know?

25 A I might have read them.

1 Q Okay. Did you rely on Mr. Dechman s advice in
2 making a decision as a director to allow Kobayashi to
3 purchase the patents?

4 A In part I relied on Mr. Dechman s; yes.

5 Q At that time, was there any discussion about the
6 640,000-dollar royalty obligation accrued on Equaphor s
7 books?

8 A That was discussed regularly in board meetings.

9 Q And was it your understanding that Equaphor would
10 then owe that \$640,000 to Kobayashi?

11 A I m not sure. We had provided for it. We were
12 recognizing it as a liability with the - we had been advised
13 that we could very well owe that. The accountants made us
14 accrue it.

15 Q You were also advised not to pay it, weren t you?

16 A That s correct; but we were acknowledging the
17 liability and taking it seriously.

18 Q And didn t Mr. Dechman say to the board that there
19 were grounds for arguing that you didn t owe the money, that
20 Equaphor didn t owe the money?

21 A I can t tell you now exactly what he said.

22 Q Okay. And did you know at the time what Kobayashi
23 was going to pay to buy the patents from International Paper?

24 A I m sorry. Would you say that again?

25 Q Did you learn at that time what -

1 A What time?

2 Q At the time you gave Kobayashi a waiver to buy the
3 patents from International Paper, did you know what the
4 financial terms were of Kobayashi s purchase of the patents?

5 A I don t recall.

6 Q You don t recall whether you knew or not?

7 A That s correct.

8 Q Do you think that s something you would have wanted
9 to know as a director in approving the waiver?

10 (Pause.)

11 BY MR. SHAPIRO:

12 Q I mean, based on your experience in business. You
13 have been a director of other companies; have you not?

14 A Yes.

15 Q Okay. I know you can t recall four years ago and I
16 don t blame you. I probably couldn t recall either. But do
17 you think that s something that as a director you would have
18 wanted - a director would want to know?

19 A I m not sure that that s a determinative item.
20 You re asking what it was costing to acquire it?

21 Q Right. I m not saying it s determinative but -

22 A I don t think it has much to do with what we re
23 talking about here.

24 Q I m not suggesting it is or isn t determinative but
25 in making the decision that the board did at that time, don t

1 believe that s a relevant factor that a director would want
2 to know?

3 A It was a very small item in relation to the
4 potential magnitude of the litigation and other things that
5 were attended to it.

6 In other words, I think you re asking me about the
7 cost of acquiring the licenses and -

8 Q I m asking you as of September 2007 -

9 A Yes.

10 Q - when Mr. Dechman came to the directors and said:
11 Equaphor is not allowed. It cannot be involved in owning the
12 patents as a condition of royalty agreements. I want to buy
13 it and I want you to waive any conflict of interest or any
14 claims there may be against me for buying it. And you as a
15 director approved the waiver agreement that was given to Mr.
16 Dechman and then given to Stein Sperling, the law firm;
17 correct?

18 A Yes.

19 Q Okay. And in deciding whether it was okay for
20 Kobayashi to buy the patents rather than maybe Equaphor
21 trying to buy the patents, wouldn t a director want to know
22 how much Kobayashi was paying for the patents?

23 A I suppose so. For all I know, I was told how much
24 they - I don t know. I told you, I don t recall the detail.
25 But I do know that the acquisition cost was prospectively

1 only a small portion of the total outlay that would have been
2
3 necessary to pursue that avenue.

4 Q Well, if you look at Exhibit I, the first paragraph
5 of the September 25 email, it says three lines from the
6 bottom that International Paper received \$200,000 in
7 guaranteed payments plus 50 percent of the net royalties
8 after expenses. Do you see that, sir?

9 A Yeah.

10 Q So, for guaranteed payment of \$200,000, if
11 Equaphor had bought the patents it could have wiped out the
12 640,000-dollar royalty obligation plus any future royalties;
13 couldn't it?

14 A I don't know whether it could or not.

15 Q Did you ask Mr. Dechman What going to happen with
16 the \$640,000 on our books if you buy the patent? Are you
17 going to try to collect it from us? ?

18 A I don't remember.

19 Q You don't remember if you did or you didn't?

20 A That's correct.

21 Q And if Mr. Dechman had said, sure as tooting I am;
22 I'm going to go right after you for the \$640,000, would you
23 have given him the waiver?

24 A I don't know how to answer that.

25 Q And ultimately, Equaphor paid \$900,000-plus to

1 Kobayashi on account of the royalties due to the fact that
2 Kobayashi owned the patents; didn't it?

3 A We've already talked about the derivation of that,
4 that number, and it really stemmed from the MSA.

5 Q Okay. Well, do you recall Mr. Dechman saying that
6 the \$3.45 million that Equaphor paid Kobayashi for these same
7 patents - 900-and-some-odd-thousand dollars of that was on
8 account of royalties that were owed to Kobayashi? Do you
9 recall him testifying to that?

10 A Yes.

11 Q Was that your understanding in September of '09
12 when you approved these transactions, that of the check that
13 Equaphor was writing to Mr. Dechman or to Kobayashi that
14 \$900,000 was on account of the royalty obligation?

15 A Yes; but that was, as we've talked about before -
16 I won't say artificially derived but it was a number that was
17 a by-product of the MSA obligation.

18 Q Well, it was the MSA obligation -

19 A You know, it was a characterization that could be
20 made properly at the time.

21 Q It was the MSA obligation plus the 900,000-dollar
22 royalty obligation, wasn't it? That's what Mr. Dechman
23 testified to. Did you understand that or was that not clear
24 to you?

25 A Okay.

1 Q Do you want me to ask the question again?

2 A You ve got me confused now.

3 Q Okay. You have been in the courtroom through last
4 week s hearing and this week s hearing; correct? Do you
5 recall that Mr. Dechman testified that the \$3.45 million was
6 made up of three components and one of them was the 900,000-
7 plus-dollar royalty obligation that he claimed Equaphor owed
8 to Kobayashi. Did you hear that testimony?

9 A Okay. Yes.

10 Q And were you aware of that when you approved these
11 transactions in September 09?

12 A Yes. Yes.

13 Q You were. Now, as I understand it, you were on the
14 board as a representative of a venture or a private equity
15 fund?

16 A That s correct.

17 Q And when had that fund been formed?

18 A In 1992 or three.

19 Q Ninety-two or three. Okay. So, in 2007, it was 15
20 years old?

21 A That s correct.

22 Q And what was the expected life of that fund when it
23 was formed?

24 A Thirteen years.

25 Q So, it was beyond its expected life?

1 A Well, actually, it had changed its form prior to
2 this time. So, it was no longer a finite life limited
3 partnership. It had become a C-type corporation.

4 Q How many investments did the fund make originally?

5 A Twenty-two; 23.

6 Q And how many were still outstanding as of 2007?

7 A Four or five.

8 Q And in 2009 how many were still outstanding?

9 A Three.

10 Q Three? One of which was Equaphor?

11 A That s correct.

12 Q Now, you approved the decision of the board to file
13 a voluntary petition for bankruptcy in December 2010?

14 A Yes.

15 Q And you were aware at that time that if the company
16 filed for bankruptcy it would take the derivative claims that
17 had been alleged in the Delaware complaint by Mr. George and
18 Mr. Bamber out of the hands of the shareholders and in the
19 hands of the bankruptcy trustee, were you not?

20 A Yes.

21 Q And what was the difference in the financial
22 condition of the company in December 2010 from, let s say,
23 October 2010? Was there any difference?

24 A Well, it was pretty well hamstrung, I guess, by the
25 derivative suit which impaired its ability to finance; and

1 so, I guess it was more insolvent sort to speak.

2 Q It had been insolvent before that and became more
3 insolvent?

4 A Well, we talked about the fact that there were
5 these, you know, increasing legal fees for the patent litigation
6 and the company actually explored whether there was some
7 way to bring further capital into the business to help
8 address those needs and the board determined that it could
9 not do so; and in my judgment, to a significant degree, it
10 was impaired by the existence of this litigation itself. So,
11 the company really had no choice. It had no way to pay its
12 bills. It had no way to respond to the litigation.

13 Q Well, as of September 2009, when the transactions
14 were completed, this company had no operating business
15 anymore; did it?

16 A That s correct.

17 Q Other than whatever cash was on hand, the only
18 asset that the company had were these patents; correct?

19 A Correct.

20 Q And the company tried to raise money in July of
21 2010; did it not? If you d look at Exhibit - I m sorry. Do
22 you recall that in July 2010, Mr. Dechman sent a letter to
23 shareholders, trying to raise money in a so-called Series G
24 offering? If I can find it, I ll give it to you. Exhibit F.
25 Is Exhibit F in front of you?

1 (Pause.)

2 BY MR. SHAPIRO:

3 Q Do you have it, sir?

4 MR. SHAPIRO: I have an extra copy. If I could
5 approach the witness.

6 THE COURT: Hand it to the court security officer.

7 MR. SHAPIRO: The court officer is bringing you a
8 copy of Exhibit F, Mr. Doherty.

9 BY MR. SHAPIRO:

10 Q You see that this is a letter addressed Dear
11 Shareholder, dated July 28, 2010?

12 A Yes.

13 Q And did you see this at the time it was sent out?

14 A I assume so.

15 Q You don t remember it?

16 A Not particularly or -

17 Q If you ll turn to the second page, there s a head-
18 ing, Series G Offering, and it reads: I have attached a
19 Series G preferred share offering term sheet that has been
20 approved by the board of directors. Do you see that, sir?

21 A I m sorry. Where am I looking?

22 Q On the second page. There s sort of a heading,
23 partway down the page, Series G Offering in bold.

24 A Yes.

25 Q And it says, I have attached a Series G preferred

1 share offering term sheet that has been approved by the board
2 of directors?

3 A Yes.

4 Q And if you look at the next page, there s the term
5 sheet. And that proposed offering didn t succeed because
6 shareholders didn t respond and sign up to buy shares; isn t
7 that right?

8 A That s my understanding.

9 Q And that was before the derivative lawsuit was
10 filed; wasn t it, sir?

11 A We already had a threatening letter from you prior
12 to the lawsuit. So, the company was clouded by your actions
13 prior to this I can assure you.

14 MR. SHAPIRO: Your Honor, if I can just note Exhibit

15 B. The lawsuit was filed August 13, 2010.

16 BY MR. SHAPIRO:

17 Q Whatever threatening letter there was didn t deter
18 Mr. Dechman from making a proposal to the shareholders to
19 raise money through a Series G offering; did it?

20 A That s correct.

21 Q And the letter doesn t refer to a threatening
22 letter from me or a derivative lawsuit or any threat of a
23 lawsuit; does it, sir? I ll let the record speak for itself
24 and the exhibit will speak for itself. I withdraw the
25 question.

1 **At the time the board of directors approved the**
2 **purchase of the patents from Kobayashi for \$3.45 million,**
3 **were you aware that there was litigation pending between**
4 **Carotex and Kobayashi?**

5 MR. McCARTHY: Objection, Your Honor. I mean,
6 relevance. The issue is, what was the trustee aware of?
7 These discussions with various interested parties -

8 THE COURT: Well, but you partially raised the issue
9 in your examination, Mr. McCarthy, that at bottom these other
10 claims have no validity. So, I guess he gets to explore that
11 they may have potential validity which you re ignoring. So,
12 go ahead.

13 BY MR. SHAPIRO:

14 **Q Do you need me to repeat the question?**

15 A Please.

16 **Q Were you aware of the Carotex-Kobayashi litigation**
17 **in September of 2009?**

18 A I certainly became aware of it. The specific point
19 in time, if - I believe we had full disclosure; and so, if
20 there was litigation underway by then, we were told about it.

21 **Q If you would look at Exhibit J in front of you, Mr.**
22 **Dechman s September 21, 2009 memo. Do you have that in front**
23 **of you, sir?**

24 A I do.

25 **Q Did you receive this from Mr. Dechman on or about**

1 September 21, 2009?

2 A I must have.

3 Q And the board voted to approve the transaction a
4 couple of days later; did they not?

5 A Yes.

6 Q And he starts out by saying: Attached are
7 agreements relating to the sale of significantly all assets
8 of MTC. This document provides some background, details of
9 the proposed deal and the resulting structure for MTC.

10 And then, if you ll turn over to paragraph three on
11 the second page, paragraph three discusses the sale of the
12 patents to Equaphor. Do you see that, sir?

13 A I do.

14 Q And that was the information that you had as of
15 September 21, 2009?

16 A I assume so.

17 Q Okay. And there s no mention of any litigation in
18 that paragraph; is there, sir?

19 A It says what it says.

20 Q Was this the first time you were advised of the
21 proposal to sell patents to Equaphor, the September 21 memo?

22 A I can t tell you about specific days in September
23 2009. We were aware of the restructuring but I can t talk
24 about any particular day or whether there was information
25 before this letter or after this letter.

1 **Q You don t recall whether you had any information**
2 **before this letter or not?**

3 A I don t.

4 MR. SHAPIRO: No other questions.

5 THE COURT: Any redirect, Mr. McCarthy?

6 REDIRECT EXAMINATION

7 BY MR. McCARTHY:

8 **Q Mr. Doherty, you referred to a letter during your**
9 **examination that you had received from Mr. Shapiro; is that**
10 **correct?**

11 A I did.

12 **Q And may I show you a copy of that letter?**

13 THE COURT: We will mark it Trustee s Exhibit B.

14 (Trustee s Exhibit B
15 was marked for identification.)

16 MR. SHAPIRO: May I see a copy of that letter, Your
17 Honor?

18 (Pause.)

19 MR. SHAPIRO: I m sorry, Your Honor. What s the
20 letter of that exhibit?

21 THE COURT: Trustee Exhibit B.

22 MR. SHAPIRO: B.

23 BY MR. McCARTHY:

24 **Q Is this the letter you were referring to?**

25 A That s correct.

1 **Q Did you receive this letter prior to the July 28,**
2 **2010 from Mr. Dechman to the shareholders about the need to**
3 **raise capital?**

4 A yes.

5 MR. McCARTHY: I would move B into evidence, Your
6 Honor. I don t have any more questions of this witness.

7 THE COURT: It will be admitted.

8 (Trustee s Exhibit B
9 was received in evidence.)

10 MR. SHAPIRO: No further questions, Your Honor.

11 THE COURT: Okay. Thank you for testifying. You
12 may stand down.

13 MR. McCARTHY: I would like to call Mr. Spiva.

14 THE COURT: Sir, if you will please come forward and
15 be sworn.

16 Whereupon,

17 CLARENCE E. SPIVA
18 was called as a witness and, having been first duly sworn,
19 was examined and testified as follows:

20 DIRECT EXAMINATION

21 BY MR. McCARTHY:

22 **Q Mr. Spiva, state your name and address, please.**

23 A Clarence Edward Spiva. The address is, 2204
24 Skylark Drive, Westminster, Maryland.

25 **Q And what is your educational background, very**

1 **briefly?**

2 A Accounting Degree from Virginia Tech. Passed the
3 CPA exam in '72. I spent a - I'm sorry. Go ahead.

4 **Q Okay. And your work background?**

5 A Twenty-two years in banking; various positions,
6 including two or three CFO positions; joined a venture firm,
7 Anthem Capital, in 1994. So, I was with venture capital
8 until about three years ago.

9 **Q And what was your position with the debtor in '07?**

10 A In '07, I was the chairman of the board,
11 represented the fund that was with Anthem Capital.

12 **Q What was the stock ownership of your venture**
13 **capital fund in '07?**

14 A It was a Series F. I'm not certain. I only
15 remember before we actually did some sales. So, it was part
16 of that 70-some percent.

17 **Q Do you recall a conversation that you and I had on**
18 **March 15**

th of this year?

19 A Yes.

20 **Q And do you recall what we talked about?**

21 A Yes. We talked specifically. One of the things
22 was about whether or not we would have purchased the patents.
23 We talked about that; and I was probably the one that made
24 the blunt statement that you referred to last week and that
25 is: From my perspective, the company had no business pursuing

1 a patent that we were going to have to sue to collect on the
2 patent, that that was not our primary business. I've been
3 there, done that and it doesn't usually come out well.

4 Q Do you recall whether we talked about whether if
5 it wanted to, legally Equaphor could have owned the patents?

6 A Yes, we talked about it. We could do it legally.
7 Was it practical? My perspective was no.

8 Q Okay. And do you recall we talked about the issue
9 of whether there was anything of a material nature that you
10 did not feel that you had considered prior to the - well,
11 in connection with the various transactions with Mr. Dechman
12 and his entities?

13 A There was nothing material that was left out for
14 me, from my perspective.

15 Q And do you have an understanding - now, the vote
16 in 09 was three to one to abstain; correct?

17 A Yes.

18 Q Mr. Evans was the abstainer?

19 A Correct.

20 Q And do you have an understanding as to whether Mr.
21 Evans has since commented or stated anything in writing as to
22 why he abstained or whether he would have voted for it?

23 MR. SHAPIRO: Objection, Your Honor. Hearsay.

24 THE COURT: I'll sustain the objection.

25 THE WITNESS: So, I can answer that?

1 MR. McCARTHY: No.

2 THE COURT: No, you cannot.

3 THE WITNESS: I couldn't remember what that - I
4 didn't know what that meant.

5 MR. McCARTHY: Okay. I don't have any more
6 questions. Thank you.

7 MR. SHAPIRO: Just a couple, Your Honor. I'm sorry.
8 Go ahead.

9 CROSS EXAMINATION

10 BY MR. MISKEN:

11 Q Please turn to Exhibit 2 in the binder and in
12 particular page eight. It's Bates 15 -

13 A I'm sorry. I can't hear you.

14 Q Page eight at the bottom of Exhibit 2 or Bates
15 stamped CAR00015.

16 A Again, where?

17 Q We're on Paragraph 8-A.

18 A Okay.

19 Q It says, Releases and Covenants Not to Suit. Do
20 you see that?

21 A Yes.

22 Q That paragraph proposes to grant you a release from
23 any cause of action that the trustee, debtor and the
24 bankruptcy estate may have; is that correct?

25 A Correct.

1 **Q And did you pay any consideration in exchange for**
2 **that release?**

3 A No.

4 MR. MISKEN: All right. I have no further
5 questions, Your Honor.

6 THE COURT: Mr. Shapiro.

7 MR. SHAPIRO: Just a few questions, if I may, Your
8 Honor.

9 CROSS EXAMINATION

10 BY MR. SHAPIRO:

11 **Q Mr. Spiva, can you see in front of you Exhibit I**
12 **which is the two emails from Mr. Dechman to the board, dated**
13 **September 26, 2007 at the top of the page and then September**
14 **25?**

15 A Exhibit I?

16 **Q Yes. It s in front of you.**

17 MR. SHAPIRO: May I ask the court officer to take
18 another copy over, Your Honor?

19 THE WITNESS: Is this Bamber Exhibit I?

20 MR. SHAPIRO: Yes.

21 THE WITNESS: Okay. I ve got it.

22 BY MR. SHAPIRO:

23 **Q Do you recall receiving this email from Mr.**
24 **Dechman, dated September 25, 2007?**

25 A I don t recall.

1 Q If you look at paragraph 1-B, do you recall I just
2 asked Mr. Doherty, asked him to read that which states, As a
3 condition of the royalty agreements, KV must not be owned or
4 associated with a competitor of the licensees and therefore
5 MTC cannot be involved. ? Do you recall being told that by
6 Mr. Dechman?

7 A I don t recall that; no.

8 Q Did you look at royalty agreements to make any
9 determination as to whether there were any legal agreements
10 that prohibited Equaphor from owning the patents?

11 A When?

12 Q September 2007.

13 A Not in September that I know of.

14 Q Well, you just testified in response to a question
15 by Mr. McCarthy that it was your view in 2007 that Equaphor
16 could have owned the patents legally. You just testified to
17 that; did you not, sir?

18 A Yes.

19 Q What was the basis for that testimony?

20 A That s what I recall, a discussion and I think it
21 went back to the summer of 2007.

22 Q You don t recall Mr. Dechman telling you that MTC
23 could not be involved or own the patents? You don t recall
24 that?

25 A No.

1 Q And one of the reasons that you didn't want
2 Equaphor to buy the patents in 2007 is you did not want
3 Equaphor to get involved in pursuing patent infringement or
4 royalty claims?

5 A I didn't want the company to get diverted from its
6 attention of its primary business to start pursuing a patent
7 litigation. That's correct.

8 Q And you also said that you've been there before and
9 you didn't think that was a good thing to do; right?

10 A That's correct.

11 Q What wasn't good about it, the expense, the time or
12 what?

13 A No. Being dead right.

14 Q Excuse me.

15 A Being dead right.

16 Q What do you mean being dead right?

17 A Being absolutely correct that there was a patent
18 infringement but it ruined us with our primary customer.

19 Q So, you had no opposition to Equaphor acquiring the
20 patents in 2009; is that right?

21 A Then it became my primary business; so, no, I did
22 not.

23 Q The primary business of enforcing royalty
24 obligations?

25 A That's right.

1 **Q Were you aware of the Carotex litigation in**
2 **September 2009?**

3 A The Carotex one?

4 **Q Yes.**

5 A I can t remember as to when I became aware of that.
6 I was only aware of one that I remember.

7 **Q One litigation?**

8 A PaperTech.

9 **Q PaperTech. You were aware of that?**

10 A Yeah.

11 **Q And at the time of the sale to Equaphor were you**
12 **told that Mr. Dechman believed he was close to a settlement**
13 **with PaperTech?**

14 A Close to a settlement?

15 **Q Yes; or that there was a settlement.**

16 A I don t recall there was a settlement.

17 **Q Well, what do you recall knowing about the**
18 **PaperTech litigation?**

19 A I remember that they were under litigation with
20 PaperTech. I did not know what the outcome was supposed to
21 be.

22 **Q And that s all you knew about litigation?**

23 A Yeah.

24 MR. SHAPIRO: Thank you. No other questions.

25 THE COURT: Any redirect?

1 MR. McCARTHY: Not from me, Your Honor.

2 THE COURT: Thank you for testifying, Mr. Spiva.

3 Okay. Is that all you have as evidence?

4 MR. McCARTHY: That s all my evidence. That s
5 correct.

6 THE COURT: Okay.

7 MR. SWAN: Your Honor, not so much of a -

8 THE COURT: Are you going to present any evidence?

9 MR. SWAN: I ll present an alternative to the case.

10 THE COURT: Well, why don t we get all the evidence
11 in and then I ll hear argument.

12 MR. SWAN: I don t think we have any evidence.

13 MR. SHAPIRO: I have nothing further, Your Honor.

14 THE COURT: Well, since it s the trustee s motion,
15 the trustee gets to make argument first and then I ll let you
16 present your alternative.

17 MR. SWAN: Okay.

18 MR. McCARTHY: Okay, Your Honor.

19 When we started, I told the court what was going on
20 here. There was a sale of assets and a compromise of mutual
21 claims and that s been explained in the testimony and the
22 evidence that s in front of you.

23 I also explained what the terms of the deal are and
24 I ll say that again very quickly. The estate will get
25 \$250,000. The buyer, which is Kobayashi, must buy up at full

1 value all of the scheduled, undisputed claims. That s a
2 total of about \$220,000. Kobayashi will be subrogated to
3 those claims and then Kobayashi also must offer the Series F
4 interests that it doesn t already own, which is about 17
5 percent, a total of about \$100,000 which represents 50
6 percent more than what had been previously, than what other
7 Series F shareholders such as Mr. Spiva s venture capital
8 fund, Mr. Doherty s venture capital fund cashed out at.

9 So, if the deal is approved, Kobayashi potentially
10 has a payout of about \$570,000; and of course, it must also
11 fund the estate s costs of litigation with Carotex, including
12 any claim objection.

13 I told the court why I thought this was a
14 reasonable deal and I don t want to go back over everything
15 that I already did but there are a couple of salient points.

16

17 The dispute with Carotex clearly is a complicated,
18 expensive piece of litigation. Carotex is saying the
19 debtor s patent rights are of no value. So, that component
20 is something that they think I apparently could give away;
21 and I ve asked them to bid on it. They weren t interested in
22 bidding on it. And I asked the derivative shareholders if
23 they wanted to bid on the patent, and they weren t interested
24 in bidding on that.

25 We also have a shareholder derivative suit that is

1 like the patent litigation, a hotly contested piece of
2 litigation; and contingency or no contingency, the issue here
3 is whether or not the trustee met a standard of
4 reasonableness in looking into these things, and based on who
5 I talked to and what I looked at - heaven knows I may not
6 have come to the same conclusion that a judge in Delaware
7 would have come to after a full piece of litigation but based
8 on everything I saw, it looked to me like it could reasonably
9 result in no recovery.

10 So, we have two expensive pieces of litigation. We
11 have Carotex saying the patent suit isn't worth anything. We
12 have shareholders basically saying the patent suit isn't
13 worth anything. Neither one of them wants to pay the trustee
14 any money to go away.

15 So, I have put this thing together which was an
16 effort, as I said in my opening statement, to balance
17 competing interests, and it is an alternative that definitely
18 results in substantial funds coming into the estate and
19 \$530,000 of claims against the estate being waived and in the
20 estate sidesetting expensive litigation.

21 In fairness to Mr. Shapiro, he offered to do that
22 on a contingency basis but a hundred percent of zero is zero,
23 and I might end up with zero. That weighed very heavily in
24 my considerations.

25 So, the question is, did I exercise my discretion

1 reasonably?

2 I guess I said in my proffer which became my
3 testimony so I can argue it now, I spent 60 hours, just up
4 to the point of the deal, in working on this; and of course,
5 it s been more time since then.

6 I talked at length with Mr. Dechman and Mr. Fiore.
7 I talked with Jeff Schwaber who is here today. He s with
8 Stein Sperling, and Bob Fletcher who is also here today; with
9 LeClair Ryan, and I considered an email from Joe Parisi who
10 is the attorney handling the Markman hearing. Mr. Schwaber
11 and Mr. Fletcher are involved in the patent litigation, as
12 well.

13 I talked and emailed with Mr. Shapiro on a number
14 of occasions. I talked with Mr. Adams about Carotex s
15 position, including the basis of its claims against the
16 debtor.

17 I mentioned in my testimony that the affirmative
18 claims by Carotex struck me as, you know, something perhaps
19 worthy of skepticism; but of course if they are -- I mean, if
20 there is anything to those claims then that s all the more
21 reason why the Series F shareholders ought to jump at this
22 deal because at least they get something out of my deal as
23 opposed to if Carotex has a four-million-dollar claim.

24 I reviewed balance sheets. I reviewed schedules of
25 payments made during the year before the bankruptcy petition.

1 I looked at attorney bills. I looked at the bylaws. I
2 looked at the asset purchase agreement, and I read the
3 shareholder derivative suit.

4 Believe me, Tom Shapiro did a very good job. He
5 raised questions in my mind from time to time. Whenever he
6 would raise a question in my mind, I would go back to Mr.
7 Dechman - you saw his demeanor on the stand -- and he had
8 what appeared to be a plausible response to me; and then I
9 did a reality check on those plausible responses, and it
10 wasn't a very lengthy conversation but I did talk to both Mr.
11 Doherty and Mr. Spiva, and I asked them was there anything.

12 This question about the email that Mr. Dechman
13 wrote that suggests that Equaphor was unable to own these
14 patents turned out to be inaccurate; and so, that was one of
15 the specific questions I asked them and they both said to me,
16 no. I think I said that in my testimony. I hope I did.
17 I was trying to ask them questions about that in my own
18 examination of them. I also asked them if there was anything
19 material that they felt they didn't know about and they both
20 said, no.

21 So, that is the position I found myself in. I
22 thought long and hard about all of this and I knew full well
23 that whatever I did was going to antagonize somebody, and
24 this is what I came up with.

25 There's no other feasible deal that's on the table.

1 Well, maybe Mr. Swan is about to come up with something
2 that s going to make us all applaud but he hasn t yet.

3 There s no other deal that s on the table, no
4 feasible deal that will definitely result in payments to any
5 of the creditors, let alone the shareholders; and now we ve
6 got these four-million-dollar claims filed by Carotex, and
7 I ve told you what effect that will have if even a small
8 portion of it is good as to the Series F shareholders.

9 Carotex talked about fraudulent conveyances, did I
10 look into that carefully enough. It just didn t seem to me
11 that that was a low-hanging fruit if everything that was done
12 was in accordance with valid contracts, with consideration,
13 and especially at a time when there - you know, there s a
14 lot of doubt as to whether the debtor was even insolvent.
15 I mean, if you look at the balance sheets, it appeared that
16 they weren t.

17 So, every which way I turned away from this deal,
18 there was a costly or uncertain or both costly and uncertain
19 piece of litigation waiting for me. So, I opted for a
20 certain global deal that potentially gets something for
21 everybody.

22 I ask the court to approve the deal on the basis
23 that it is a reasonable reconciliation of competing interests
24 in the case, that no one has come along with a better deal
25 that results in a certainty of claims being paid, money in

1 the estate, \$530,000 of claims against the estate being
2 waived, and that the alternatives are uncertain and
3 potentially expensive.

4 As I have mentioned several times, if the court
5 does approve the deal, I want to add some clarifying language
6 that the three paid-up licenses aren't affected. The
7 trustee - and I guess we would say something about any
8 license rights of Carotex, as well, and that the trustee is
9 releasing Whiteford Taylor from any avoidance claims because
10 that was a condition of their withdrawing their limited
11 objection even though I had gone through the payments to
12 professionals. I thought they had a pretty good new-value
13 defense.

14 Finally, I would point out that throughout this
15 case, at least by the end of '09, Mr. Dechman and Mr. Fiore
16 are 83-percent equity owners of the company. So, yes, I
17 suppose it might have benefitted them more to be dealing
18 through an entity in which they owned - actually, I think it
19 was 80 percent as opposed to 83 percent.

20 But you know, considering everything, their
21 significant ownership of the company and all of the people I
22 talked to and all the other documents that I reviewed, I
23 submit that I acted within the ambit of my reasonable
24 discretion.

25 Thank you.

1 THE COURT: Let me hear from Mr. Swan.

2 MR. SWAN: Thank you, Your Honor.

3 Rule 9019 cases require in evaluating settlement
4 four factors: One is the consideration of the probability
5 of success in litigation. Number two, consideration of the
6 difficulties if any to be encountered in collection. Number
7 three, consideration of complexity of litigation involved and
8 the expense, inconvenience and delay associated with the
9 litigation, and, number four, consideration of the paramount
10 interest of creditors and a proper deference to their
11 reasonable views. I ll take those factors in reverse order.

12 First, the paramount interest of creditors and a
13 proper deference to their reasonable views. I emphasize
14 deference to creditors, the paramount interest of creditors.

15 It was striking that all of the trustee s testimony
16 was: I talked to Dechman. Dechman told me this. The debtor
17 told me this. The so-called dog and pony show which I m sure
18 is an accurate description of what it was.

19 The trustee has only been considering the interests
20 of the debtor and its insiders and excluding the interest of
21 the creditors, Carotex, the shareholder claims. That s not
22 the way this is supposed to work. That s not appropriate.

23 Secondly, the complexity of the litigation and the
24 expense, inconvenience and delay. That s easy. The solution
25 there is the Shapiro firm which the trustee testified is

1 willing to handle the case. Complicated as it is, they re
2 willing to handle the case on a contingency and advance
3 expenses.

4 THE COURT: Well, there are two expensive pieces of
5 litigation. One is the derivative suit. The other is your
6 client.

7 MR. SWAN: Which they would be willing to handle;
8 but our walk-away offer that was attempted between hearings,
9 after the hearing last week, would take care of that because
10 Carotex would waive any claims against Equaphor. More on
11 that later.

12 The third factor for settlement is difficulty in
13 collection. The trustee testified that this was not a
14 consideration because the potential insider defendants could
15 pay. So, that factor also weighs in favor of not releasing
16 them.

17 Finally, the probability of success. There are, we
18 believe and Mr. Shapiro believes, significant claims against
19 the insiders, up to 14 million altogether, according to the
20 shareholder objections. But 250,000 is just simply too
21 little settlement consideration for the releases.

22 The testimony I think confirms that the trustee
23 gave very little emphasis to the value of the Chapter 5
24 claims and what he would be giving up with those releases,
25 relatively little analysis of the documents, no analysis, he

1 said, as to whether the insider claims could be subordinated
2 although I think he said in his testimony last week that they
3 likely could be subordinated. The trustee simply, again,
4 deferred to the debtor on their evaluation of the case.

5 There s no explanation whatsoever as to why Stein
6 Sperling should be released for no consideration at all.
7 They are offering no separate consideration.

8 In fact, almost all the released parties are
9 offering no separate consideration for the releases. So,
10 we submit there is no success with this sale to meet the test
11 in favor of settlement.

12 There s a significant public policy concern over-
13 riding all this. The way bankruptcy cases are supposed to
14 work is that the trustees are supposed to use avoidance
15 actions, to call back improper payments, to benefit all
16 creditors particularly when the payments are to insiders.
17 That s why, for example, the preference look-back period is
18 one year with insiders and 90 days with respect to non-
19 insiders. There s a policy to scrutinize insider
20 transactions.

21 The trustee should not sell assets to insiders
22 without heavy scrutiny. That s why in many cases where sales
23
24 are larger transactions to insiders the courts will often
25 appoint an examiner to investigate the transaction because

1 it s given more scrutiny.

2 Here the patents are being sold to the same entity
3 that sold the patents to the debtor for three and a half
4 million dollars less than two years ago. Here the debtor in
5 2008 was an eight-million-dollar-a-year business that
6 proceeded to give away its assets to the insiders.

7 The facts are complicated but the bottom line is,
8 liquidating dividends were given to shareholders when there
9 were creditors. This was all controlled by Mr. Dechman who
10 was the debtor designate in this case; but at least given
11 these transactions, he should have resigned that role.

12 This transaction cannot be approved and the estate
13 does have better alternatives.

14 The trustee has said that there was an opportunity
15 for Carotex to bid on the patents. That s not really the
16 case. The sale was certainly not set up to receive
17 alternative bids. This is being done as a private sale.

18 So, after the hearing last Tuesday, we explored
19 some ideas with the trustee. He deferred to Kobayashi. So,
20 we weren t able to get anything done.

21 But I talked to my client over this weekend and
22 this morning. We have an offer. It s not competing bids,
23 sort to say, but it s something designed to match the
24 Kobayashi offer without the insider releases; and Mr.
25 Dechman s testimony, by the way, was that Kobayashi is not

1 willing to purchase the patents unless he gets the releases.

2 Well, we are.

3 We will pay \$250,000 for the patents, including
4 license agreements, including the right to recover for all
5 past infringements. In other words, we will pay \$250,000 for
6 the patents and the patent rights.

7 Number two, the Stein Sperling preference that the
8 trustee wants to release, if he doesn't want that we do; and
9 we can figure out how to structure that. We would love to
10 have standing to pursue that preference case. If that's not
11 possible, we can figure out a way to do it: Put it into a
12 trust where we get assignment of the proceeds but as long as
13 we have some control over the litigation, again preferably
14 standing to pursue it ourselves. If the trustee doesn't want
15 it, we want it.

16 Third, we will waive our claims against the estate.
17 We filed unliquidated claims. We estimated them at \$4
18 million or up to \$4 million on the proof of claim filing. We
19 will waive those so there's no issue with an estate expense
20 of defending my client's claims. We'll give those up. No
21 releases.

22 So, the estate with Mr. Shapiro on contingency or
23 some other way of doing it can pursue the Chapter 5 actions
24 against Monitoring Technology, Mr. Dechman and all the rest;
25 Kobayashi.

1 So, again, it s not an auction. It wasn t set up
2 as an auction. It s not a competing bid. This is merely
3 achieving a result that matches the sale consideration with
4 this deal but keeps the most valuable assets of the estate,
5 the Chapter 5 actions in the estate, and it eliminates the
6 public policy concerns, the overall outrageousness of the
7 insider releases. I don t think anyone could put a value on
8 that but I don t think any sale could be approved that gives
9 those away.

10 Thank you. Any questions?

11 THE COURT: Not at this point.

12 MR. SWAN: Thank you.

13 THE COURT: Thank you.

14 Mr. Shapiro.

15 MR. SHAPIRO: I want to thank you for Your Honor s
16 patience. I know we ve gone way over the time you said you
17 wanted to devote to this.

18 I don t want to suggest any lack of confidence in
19 my opposition to the motion but I do want to raise one point,
20 Your Honor, in the event Your Honor doesn t reject the
21 motion. I have to do that for my clients. They ve
22 offered - and Mr. McCarthy keeps referring to this - to buy
23 out the minority Series F interest for \$100,000 which is
24 really a pittance compares to what my clients - and I
25 represent a number of Series F holders, not just Mr. George

1 and Mr. Bamber. But the offer is, of course, conditioned on
2 the sale being approved and Mr. Dechman, et cetera giving up
3 their releases.

4 They have recused my request that the offer be
5 kept open until after the court rules on this; and if the
6 court rules against us then I guess the white flag goes up
7 and my clients would go ahead and surrender their shares.
8 But we shouldn't be put to the Hobson's choice of having to
9 make that election before Your Honor has ruled because that's
10 certainly not their choice.

11 Their choice is they want to go forward with the
12 derivative litigation. It would not be derivative at that
13 point. It would be a trustee's litigation. They've put
14 together a war chest to do this and they really feel very
15 strongly about it, and I feel I should raise that.

16 I would ask that the court insist on that as an
17 amendment to this agreement if the agreement does get
18 approved.

19 It seems to me, Your Honor, and you obviously
20 brought it up a moment ago, that the only possible - and I
21 don't say it is a justification but the only possible
22 justification for this deal is that Mr. McCarthy is in a
23 difficult position of having this expensive Carotex
24 litigation without the funds to defend it.

25 But the fact of the matter is that he never

1 approached Carotex or never explored with Carotex the idea
2 of both parties walking away.

3 You ve heard Mr. Spiva s testimony. It certainly
4 would be in the interest of this company to agree with
5 Carotex: We ll drop all our claims against you. You drop all
6
7 claims against us. And if that were to happen then it s
8 there for the trustee to take. It s there for the taking,
9 either a walk-away or the 250,000-dollar offer.

10 If you were to pursue that option and that s an
11 available option then the only justification for this
12 transaction, that I have to find a way to defend the Carotex
13 litigation, simply disappears.

14 This company has no obligations, no creditors other
15 than the very law firms who have been defending Mr. Dechman
16 and Kobayashi and Equaphor jointly and who have been billing
17 all of their work for the past year to the tune of some
18 \$800,000 to Equaphor. I mean, talk about an injustice to
19 this debtor, to this estate; and Mr. McCarthy acknowledged
20 that he never really looked into whether or not Kobayashi and
21 Dechman were paying for their legal fees, or any part of
22 these legal fees, and Mr. Dechman acknowledged on the stand
23 that they had not.

24 So, you ve heard all about the Management Services
25 Agreement and the sale incentive fee. I won t repeat that

1 but I think it s a very important part of this whole
2 situation and it s very important to my clients, just to
3 review the unbelievable history of the patents and how this
4 company has been abused from beginning to end.

5 Mr. Dechman bought the patents for \$200,000 plus
6 the obligation. If he collected royalties, he had to pay 50
7 percent of the royalties after deducting the expenses for
8 collecting them. So, \$200,000, and it would have wiped out a
9 640,000-dollar royalty obligation, at the time when this
10 company had money and could easily have paid that.

11 And at the end of the day, Mr. Dechman who took the
12 position that under the most favored nation provision, the
13 company didn t owe the money, and recommended the company not
14 pay the money to International Paper which had not pursued
15 the money - two years go by. He increases the royalty
16 accruals saying, you now owe my company \$900,000, and he
17 extracts \$900,000 from this company in September 2009 as part
18 of this series of transactions in which he unloaded the
19 patents onto Equaphor.

20 I asked Mr. Dechman on the stand: You had a win-win
21 situation, didn t you, if at the time you sold the patents to
22 Equaphor - you got the PaperTech settlement which was in the
23 works and you had hoped that Carotex would follow suit. Then
24 the settlement with Carotex - the proceeds would be paid to
25 Kobayashi under the terms of the patent purchase agreement

1 that he admitted, included the provision - not only was
2 Kobayashi paid three million, 450, but Kobayashi got paid
3 anything that was collected in the next year.

4 So, the \$690,000 from PaperTech was paid over to
5 Kobayashi. That takes you up to four and a half million
6 dollars, a little over four and a half million dollars, plus
7 if they recovered something from Carotex that money would go
8 to Kobayashi.

9 But if the hope and expectation did not come to
10 past and they continued to be embroiled in this litigation
11 then they managed to offload the litigation expense onto
12 Equaphor, and it adds up to some 800-and-something thousand
13 dollars that Equaphor has paid, and Mr. Spiva, the director,
14 approved this without even knowing about the Carotex
15 litigation. This was a director who was of the view: You
16 don't want anything to do with patent litigation. I've had
17 bad experience with it in the past. That's why I didn't want
18 this company to buy the patents in the first place and I
19 blessed Kobayashi buying them. And he either just overlooked
20 that because he does whatever Mr. Dechman wanted or he was
21 ignorant of it and it wasn't disclosed to the directors that
22 they were acquiring a real albatross.

23 Equaphor was never a party to the Carotex litiga-
24 tion. It was only when Mr. Dechman or Kobayashi sold the
25 patents to Equaphor. Then they moved to substitute Equaphor

1 as a party and Carotex filed a second amended declaratory
2 judgment action which is in their exhibit book, which added
3 Equaphor as a defendant.

4 So, they managed to do this win-win situation and
5 burden this company, which had no operating business anymore,
6 no interest in the patents, no use for the patents, with the
7 expensive Carotex litigation.

8 What really adds insult to injury, Your Honor, is
9 according to Mr. Dechman s own memo - this is Exhibit F, a
10 letter to the shareholders - this company was insolvent in
11 July of 2010. The language is right in there, on the second
12 page.

13 Mr. Dechman also wrote in this July 28, 2010
14 letter, Exhibit F, and it says, If the company is unable to
15 obtain capital it will be deemed insolvent and will cease
16 operations.

17 Under the terms of the Kobayashi note - that s
18 the 500,000-dollar note that was part of the patent sale -
19 the insolvency and payment default will trigger a reversion
20 of the patents back to Kobayashi. So, apparently Kobayashi
21 could have taken the patents back.

22 A derivative suit gets filed against them in
23 August, August 13th. We have a settlement meeting in October.
24
25 I get together with my clients. I make a formal demand in

1 November. They take it up at a December 7 board meeting.

2 The minutes are now an exhibit. They take it up. They
3 characterize the demand as outrageous and start exploring
4 bankruptcy.

5 Then they put this company into bankruptcy and no
6 witness could say that this company is in any different
7 financial condition in December than it was previously.

8 They put it into bankruptcy for the purpose of
9 trying to avoid the derivative litigation when they could
10 have taken the patents back themselves, and they forbore
11 from doing that so that Equaphor was continuing to pay the
12 bills.

13 Now they have this agreement where they re going to
14 get the patents back with the benefit of a million dollars in
15 legal fees having been paid and the litigation that much
16 further along.

17 So, sort of the proof in the pudding, to tie all of
18 this together, is: Mr. McCarthy testified they would not
19 purchase the patents unless they got a release on the
20 derivative claims. I mean, it just gets very obvious what
21 the game is here.

22 This company would have been much better off if
23 back in September 2009 - and I say, I think the testimony
24 makes it clear that there was not a sale of all or
25 substantially all of the assets. They sold the business to

1 Cognex. The board rejected the idea that there could be more
2 than one transaction to make up the sale, to qualify for the
3 sale incentive fee; and then they buy the rest of the assets
4 themselves and say, aha, at a bargain basement price, at a
5 million-five for 70 percent of the business. And they say:
6 Well, now we've sold all the assets. So, we're entitled to
7 the sale incentive fee. And it reverse engineers and that
8 justifies the million and a half purchase price. It
9 justifies giving you the patents and we take \$3.45 million.

10 They could have just taken the three million, 450
11 and kept the patents and this company would still have had
12 another million dollars in the bank that it could have
13 distributed to shareholders. But no. They've unloaded all
14 of the patents for all the reasons that I've just explained.

15 The thing now comes full circle when they say, we
16 want the patents back but only if you release us from the
17 derivative claims.

18 They could get a release from the derivative
19 claims, take the patent back, agree to the same walk-away
20 with Carotex and just laugh all the way to the bank.

21 I would ask Your Honor for all these reasons to
22 reject the motion.

23 Thank you.

24 MR. REYNOLDS: Your Honor, if I may just address the
25 court briefly. I'm not going to reiterate what Mr. McCarthy

1 stated previously in his closing but I would like to address
2 the issue of this offer that has just come to light literally
3 at the eleventh hour.

4 This is an offer that Carotex could have made weeks
5 ago, if not from the beginning of the case. They ve known
6 about the trustee s discussions with my client for several
7 weeks. They filed a motion for relief from stay. They have
8 been the ones that have been pushing the schedule here,
9 saying that the court has to lift the automatic stay so that
10 we can go back up to New York and litigate the validity of
11 the patents and the claims.

12 They filed a four-million-dollar claim on Friday on
13 behalf of ECS; they filed another four-million-dollar claim
14 on behalf of Carotex on Friday, and then today at the
15 eleventh hour come in with an offer of \$250,000. It s not
16 a competitive offer with what the trustee has brought to the
17 court.

18 All they re offering is \$250,000 and a waiver of
19 their claim. What Kobayashi has offered is \$250,000. Their
20 claims are gone. Kobayashi undertakes the administrative
21 expenses, the estate s administrative expenses to pursue the
22 claim litigation up in New York. That \$250,000 remains as a
23 pot of money for the payment of the claims in this case and
24 the trustee does not come out of pocket in terms of
25 litigating up in New York, and we will have a resolution as

1 to what the genuine claim for Carotex is.

2 It s rather gamesmanship at this point to come in
3 at this late moment with this offer. It is not a comparable
4 offer in connection with what Kobayashi has made. The
5 Kobayashi offer keeps the \$250,000 in the estate and allows
6 for the litigation of the Carotex claim.

7 It s clear from the trustee s testimony that he has
8 investigated all of these issues, that he has talked not just
9 to the Kobayashi affiliates but he has talked with Mr.
10 Shapiro; he has talked with the Carotex and the ECS counsel;
11 he has looked into the solvency issue; he has looked into the
12 Chapter 5 claims, and he has decided that this is a fair
13 purchase for the assets. It allows or eliminates administra-
14 tive expenses in this case.

15 Your Honor, it s a fair offer. The court should
16 accept the offer.

17 If the court is interested in the Carotex offer, we
18 should be given an ability to respond to that offer; but at
19 the end of the day, the Kobayashi offer is the fair offer and
20 it is the one that this court should accept.

21 Also, Your Honor, what has also been raised in
22 terms of an issue of good-faith purchaser - and Kobayashi,
23 if the court approves the sale, would be a good-faith
24 purchaser and the court should enter an order allowing them
25 to be deemed a good-faith purchaser.

1 The case law provides, and I m citing the Kibbis
2 case at 764, F.2nd, 1019 out of the 4th Circuit in 1985, that
3 in order to destroy the good-faith purchaser position there
4 would have to be misconduct that is tantamount to fraud,
5 collusion between the purchaser and other bidders and the
6 trustee or an attempt to take grossly unfair advantage of
7 other bidders. None of that has happened in this case.

8 There has been no evidence offered from any other party.

9 There has not been any bidder in this process prior to this
10 for collusion to occur.

11 So, my client, Kobayashi, would be a good-faith
12 purchaser under the terms of this agreement. We would ask
13 that the court, if the court approves this sale, allow for
14 them to be deemed a good-faith purchaser.

15 THE COURT: This matter is before the court on a
16 motion by the Chapter 7 trustee to approve a sale of assets
17 and compromise of claims.

18 The debtor in this case, Equaphor, Inc., filed a
19 voluntary Chapter 7 petition in this court on April 26, 2011
20 and Kevin McCarthy, an experienced trustee, was appointed as
21 a Chapter 7 trustee.

22 At the time the case was filed, Equaphor was
23 involved in two pieces of litigation. One was related to
24 patents although there are monetary claims for alleged misuse
25 of patents with two companies called Carotex, Inc. and Event

1 Capture Systems in the Southern District of New York.

2 This litigation had actually originally been
3 brought against an entity called Kobayashi Ventures, LLC but
4 in the middle of the litigation Kobayashi transferred or sold
5 the patents to the debtor as part of a larger transaction,
6 very complicated - I have heard a lot of testimony here -
7 that effectively took place in two stages, 2007 and 2009.

8 The patents in question had originally belonged to
9 International Paper and the debtor here was a licensee of the
10 patents, and there was some dispute over the amount of
11 royalties owed and at that time the board of directors
12 allowed the insiders of the company to set up this separate
13 entity, Kobayashi Ventures, LLC, to acquire the patent from
14 International Paper.

15 As part of the subsequent transaction, the assets
16 of the debtor were sold off. Part of it was sold to a third-
17 party purchaser, Cognex, and the remaining assets were sold
18 to an entity again set up by the insiders called Monitoring
19 Technology, LLC, leaving the debtor here with no assets. It
20 had about \$500,000 in cash, according to the evidence that
21 has been presented, but it then acquired the patents which
22 were the subject of this increasingly expensive litigation up
23 in New York so that all it had effectively were the
24 liabilities related to the patent litigation which was then
25 heating up.

1 A lot of this led to the second piece of litigation
2 and that is that two of the shareholders of the corporation,
3 Harry George and Frederick Bamber, brought a shareholder
4 derivative suit against the directors and officers. I forget
5 whether Kobayashi was a defendant in that matter but it
6 doesn't really matter.

7 Immediately, apparently, the targets of the
8 shareholder derivative suit demanded indemnification from
9 the debtor under its bylaws and the debtor found itself
10 without money and unable to litigate either the New York
11 patent litigation or to continue providing indemnity to its
12 officers and directors; and accordingly, the board voted to
13 authorize a Chapter 7 filing.

14 Then the same folks who are the targets of the
15 derivative suit have put together an offer to the trustee
16 which is presently before the court to purchase all of the
17 patent rights for \$250,000, as well as to purchase from him
18 all of the shareholder derivative claims. Of course, upon
19 the filing of the Chapter 7 petition, any derivative claims
20 really pass to the Chapter 7 trustee. So, the trustee has
21 proposed to sell both of those, the shareholder derivative
22 claims and the patent claims, back to Kobayashi, the very
23 entity that sold it to the debtor.

24 But coupled with the sale is a sweeping set of
25 releases of anyone who has ever had any connection with the

1 debtor, releases of the debtor s attorneys who represented it
2 in the patent litigation, releases of all the directors and
3 folks connected with the shareholder derivative suit.

4 Now, I really have a great deal of admiration for
5 what Mr. McCarthy has attempted to do here. I think based on
6 the testimony, he has looked at the whole situation; and if
7 the proposed settlement were to be judged purely on economic
8 grounds, putting aside the last-minute offer made during
9 closing argument by Carotex to purchase the patent claims
10 alone without any releases for \$250,000, putting that aside,
11 I think that you would have to say, judging from a purely
12 economic point of view, that Mr. McCarthy has put together a
13 package which may not entirely succeed but certainly attempts
14 to balance the competing interests in the case.

15 My fundamental problem though is, I think the scope
16 of these releases is just contrary to public policy, that
17 Congress never intended that Chapter 7 filings could be used
18 as a method by which targets of a shareholder derivative suit
19 could take the company into bankruptcy and then buy those
20 claims outside of bankruptcy.

21 Corporations don t get a discharge in bankruptcy
22 and nobody else gets to ride on a discharge even if one is
23 granted but here everybody is getting releases who arguably
24 has any liability to the estate and I just think that that
25 was not what Congress intended Chapter 7 to accomplish.

1 I think this comes close to a bad-faith filing, to
2 be very frank; and one of the things I have considered is
3 whether I should sua sponte dismiss this case as a bad-faith
4 filing but I m not going to do that but I am also not going
5 to approve this proposed sale and compromise.

6 So, I will prepare the order denying the trustee s
7 motion to approve the sale.

8 I have to say that the last-minute offer by Carotex
9 to purchase the patent claims which would eliminate the only
10 source of cash drain on the estate because counsel for the
11 derivative suit plaintiffs has agreed, if the trustee is
12 willing, to represent the estate on a contingency-fee
13 basis - if the Carotex matter were settled by Carotex s
14 purchase of the patents then the dilemma the trustee has
15 found himself in, and it has been a real dilemma, of being
16 party to some very expensive litigation without any ability
17 to fund it would just simply go away.

18 I was actually prepared to make a final ruling on
19 the relief from stay but I think that I probably ought to
20 give the parties at least two weeks to determine whether the
21 trustee wants to accept Carotex s offer which if accepted
22 would eliminate any need for the Markman hearing to go
23 forward in New York and thus resolves the relief from stay,
24 as well.

25 So, what I m going to do on the relief from stay,

1 I am going to continue that over to my May 18 relief from
2 stay docket at 9:30 and we will see where we stand then.

3 We will stand adjourned.

4 (Whereupon, at approximately 4:15 p.m., the
5 proceedings were adjourned.)

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UNITED STATES BANKRUPTCY COURT

T R A N S C R I B E R ' S C E R T I F I C A T E

Diversified Reporting Services hereby certifies that:

(A) The foregoing pages represent an accurate and complete transcription of the proceedings, before the United States Bankruptcy Court, the Honorable Stephen S. Mitchell, Judge, presiding, in the matter of EQUAPHOR INCORPORATED (debtor), and (B) these pages constitute the original transcript of the proceedings.

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